STUDENT'S HANDBOOK OF ACCOUNTING

SOLUTIONS TO QUESTIONS IN THEORY OF ACCOUNTS, PRACTICAL ACCOUNTING, AND AUDITING CONTAINED IN

ELEMENTS OF ACCOUNTING

FOR THE USE OF
TEACHERS, STUDENTS, AND
PRACTICING ACCOUNTANTS

BY

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PREFACE

"Elements of Accounting" was published in June, 1913. As stated at that time, it was written mainly "to bridge the gap between bookkeeping and accounting." That it has filled a real need is evidenced by the friendly reviews and comments of accountants, teachers, and lay critics. The hearty reception which has been accorded to it has necessitated three editions within a period of about a year and a half.

At the request of many students and teachers, the publishers arranged with the author to produce authoritative solutions to the practical exercises appended to the respective chapters in "Elements of Accounting." To enhance the value of these solutions they have been cast into what may be termed C. P. A. form. Moreover, there have been included references for those who wish to make a further study of the points treated in the different solutions. This supplementary research material has been included in the belief that it will be welcomed by the ambitious student.

This handbook should be used in connection with "Elements of Accounting." Such correlation, however, is not *absolutely* essential because of the fact that the exercises of the accounting text have been incorporated in the present volume. For obvious pedagogic reasons, each question is immediately followed by its answer or solution. The solutions to Groups II will probably be employed by many as much for the forms displayed and illustrated, as because they constitute solutions to specific practical accounting problems. The entire volume may be employed as a special or supplementary text in Accounting.

The author of "Elements of Accounting" has aimed to inspire the student of accounting with the realization that the subject is a growing one, and that it has not yet crystallized sufficiently to produce fixed terminology and forms. His ideal has thus far met with friendly reception. On the other hand, many students have asked for some fixed definite standards by which to measure their own solutions of accounting problems. It is in sympathetic appreciation of the needs of these ambitious students that the present text is now offered. It must be recognized, however, that though in the opinion of the author the various forms and solutions offered constitute acceptable C. P. A. and Civil Service answers, in many cases other solutions and forms may be equally acceptable.

One of the recognized needs of accounting training in America is a means of extending definite and concrete aid to students preparing for public accountancy and for the various state examinations for certified public accounting. Greendlinger's "Accountancy Problems and Solutions" has done much to meet this demand, and the Students' Department of the *Journal of Accountancy* has contributed its aid, but much still remains to be done in this comparatively new field. It is sincerely hoped that this book will not only greatly enhance the value of "Elements of Accounting," but that it will also widen the opportunities now available to the student of accounting.

J. J. K.

New York, March 10, 1915.

CONTENTS

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STUDENT'S HANDBOOK OF ACCOUNTING

SOLUTIONS TO EXERCISES

CHAPTER II

ACCOUNTING

Group One

1. *What kind of service does the accountant render the business community?*

1. The accountant organizes the books of concerns so as to make possible the obtaining of maximum information at a minimum expenditure of time and cost. At times, too, in practice, he audits the records made in the books by the bookkeeper for the purpose of establishing their accuracy and correctness, as well as for the purposes of preparing final statements so as to determine the condition and progress of the business. As a cost accountant, he determines the unit costs which are so essential to the executive in maintaining business efficiency. He also prepares reports for executors and trustees, and is frequently called upon as a business counselor.

(Pp. 19–20.)

2. *Define Controlling Accounts, and illustrate by means of Accounts Payable.*

2. Controlling Accounts are summary accounts in the General Ledger. They summarize or control many accounts in a subsidiary ledger. The most common examples are Accounts Receivable and Accounts Payable. Accounts Payable Controlling

Account, Creditors' Ledger Controlling Account, or Accounts Payable, is the name of the Controlling Account in the General Ledger which controls the Creditors' or Purchase Ledger. The manner of control is illustrated as follows:

(*a*) The individual purchases entered in the Purchase Book are credited to individual accounts in the Purchase Ledger, while the total is carried to the credit of Accounts Payable account in the General Ledger.

(*b*) Payments made to creditors are entered on the credit side of the Cash Book. If payment is without discount, the amount is entered into the Accounts Payable column and the Net Cash column. If discount has been allowed us, then the amount entered in the Net Cash column plus the amount entered in the Discount on Purchases column, is equal to the amount entered in the Accounts Payable column. The individual items in the Accounts Payable column are charged to the separate accounts in the Purchase Ledger, while the total is charged to the Accounts Payable Account in the General Ledger.

(*c*) Returns by us and notes given by us are entered in the Journal. In both cases, individual accounts in the Purchase Ledger are to be charged. These items are entered in a debit column of the Journal, headed Accounts Payable. Corresponding to the individual debits to the Purchase Ledger, resulting from the items entered in this column, the total column, monthly, is charged to the Accounts Payable Account in the General Ledger.

It should be clear, therefore, that inasmuch as a summary entry in the Accounts Payable Account of the General Ledger is made monthly to correspond to the individual daily postings to the individual accounts in the Purchase Ledger, that at any given moment of time, when all postings have been completed, the balance of the Accounts Payable Account in the General Ledger should exactly equal the sum of all the balances of all the accounts in the Purchase Ledger.

(*Other Uses of the Controlling Account.*—Besides acting as a summary and a control as above indicated, the controlling account is a very useful device in that it makes possible the taking off of a Trial Balance from the General Ledger in a very short time. Moreover, it acts as a control not only because of the check on the balances in the subsidiary ledger, but also in the following way: The sum of all the charges to the controlling account should equal the sum of all the debits in the Purchase Ledger. Similarly, all the credits of the controlling account should equal the sum of all the credits to all of the accounts in the subsidiary ledger. In case of error, that is, in case the controlling account does not agree with the sum of all the balances of the auxiliary ledger, and the ordinary checking has been performed, then the fact that the debits of the Controlling Account should equal the debits of the subsidiary ledger accounts, proves a very potent aid in localizing the error or errors.)

(Pp. 31–35; Chap. II); M. & R., Chap. XXIV; M., 251–2; J., Vol. 9, 29–35.

3. *What is meant by a contingent liability? How may such a liability be extinguished?*

3. A contingent liability is one that exists in virtue of the fact that a concern has obligated itself by endorsing a note, "going" on a person's bond, acting as surety, etc. In other words, it means the assumption of a *potential* liability which becomes *actual* in the event of some contingency arising. This contingency, in the cases already mentioned, would exist if the note went to protest, if the person bonded proved dishonest, or if the person for whom it acted as surety failed in the performance of his contract. A contingent liability is extinguished in one of two ways: if the contingency does not arise, it is extinguished at the expiration of the time involved; if the contingent liability becomes an actual one, it may be extinguished by fulfilling our obligation. Some cases of contingent liability, stated under the topics of guaranty and warranty of Commercial Law courses, are ex-

tinguished by any changes made in the conditions without the knowledge and consent of the person who assumes the liability. (For further information on this subject consult law texts.)

(P. 30); M., 165–170; G., II, 208–211; H., 32, 192.

4. *Criticize the Merchandise Account as ordinarily kept, and suggest a remedy.*

4. The criticism is based upon Professor Sprague's stricture to the effect that an account which has to be made over should have been made right at first. The Merchandise Account as frequently kept is a mixed account; it contains real elements (original and final inventory) together with nominal items such as sales, sales returned, purchases and purchases returned. The remedy is to employ three or five separate accounts:

(*a*) Merchandise Inventory Account.
(*b*) Purchase Account (or sometimes this account and Purchases Returned Account).
(*c*) Sales Account (and, sometimes, Sales Returned Account).

(Pp. 23–28); B., 117–118; G. I, 185; S P., 155–161.

5. *Classify the following accounts as Personal, Real, or Nominal:*

(*a*) *Insurance;* (*b*) *Mortgage Payable;* (*c*) *T. Jones, Prop.;* (*d*) *Returned Sales;* (*e*) *Wages;* (*f*) *Taxes;* (*g*) *Patents;* (*h*) *Investments.*

5. (*a*) Insurance—Nominal Account.
(*b*) Mortgage Payable—Real Account.
(*c*) T. Jones, Prop., is sometimes regarded as a personal account, but is really a peculiar account which should be called Proprietorship.
(*d*) Returned Sales—Nominal Account.
(*e*) Wages—Nominal Account.

(*f*) Taxes—Nominal Account.
(*g*) Patents—Real Account.
(*h*) Investments—Real Account.

(Pp. 20–21); G. A., 7–8; B., 21–27; 85–94; H., 6–10; W. A., 50–52; E., Chap. XII.

Group Two

1. *Construct a chart to show various per cents. of profits on investment for eight years. Use your own figures.*

1. No form is submitted, for obvious reasons.

(Pp. 36–39); M., 230–240.

2. *Make entries in your books for the following transactions:*

July 31, 1913. Sold to R. Rollins & Bros., 600 yd. Am. Woolen at $1.12^{1}/_{2}$, terms 1%, 30 da.; 4 mo. net.

Nov. 30, 1913. Received their three months' note with interest at five per cent. in full.

Dec. 12, 1913. Discounted note at First National Bank. (The note was duly paid at maturity.)

(Solution on page 6.)

3. *L. L. Longley buys from and sells to us. On Nov. 30 his balance in our Sales Ledger is $500.00, while the balance in the Purchase Ledger is $200.00. We receive, accept, and enter his check of $300.00 in full settlement of account. Show entry for check and subsequent adjustment entry, in all books of original entry affected.*

(Solution on page 7.)

2. (Question on page 5.)

L. F.				
		JULY 31, 1913		
	R. Rollins & Bros.	600 yd. Am. Woolen @ $1.12½	675.00	
	To Sales	1/30, 4 mo. net		675.00
		NOVEMBER 30		
	Notes Rec.		675.00	
	To R. Rollins & Bros.	Their 3-mo. note with interest at 5%		675.00
		DECEMBER 12		
	Cash	Discounted R. R. & Bros. note at	674.56	
	Discount on Notes	First National Bank	.44	
	To Notes Rec. Discounted			675.00
		FEBRUARY 28, 1914		
	*Notes Rec. Discounted	R. R. & B.'s note duly paid at maturity	675.00	
	To Notes Rec.			675.00

*This entry is usually made either a few days after maturity, or more frequently, at the end of the month in which maturity occurs.

(P. 30); G., I, 93; G., II, 226–227.

3. (Question on page 5.)

Cash Book Receipt Side

				Accts. Rec.	Dis. on Sales	Net Cash	General
Nov.	30	L. L. Longley	Check in full of a/c	300.00		300.00	

Journal

Notes Rec.	Accts. Pay.	General	L. F.		General	Accts. Rec.	Notes Pay.
				NOVEMBER 30			
	200.00			L. L. Longley To L. L. Longley Balance of a/c in Purchase Ledger, $200.00; balance of a/c in Sales Ledger, $200.00; this entry is made for the purpose of adjusting the balances.		200.00	

SOLUTIONS TO EXERCISES

CHAPTER III

THE APPLICATION OF ACCOUNTING TO BOOKKEEPING

Group One

1. *Mention the names of three extra columns in the Cash Book. Tell regarding one of them all of the advantages connected with its use.*

1. (*a*) Discount on Sales column, debit side of Cash Book.
(*b*) Discount on Purchases column, credit side of Cash Book.
(*c*) Expense column, credit side of Cash Book.
(*d*) The advantages connected with the use of these three columns (students are required to give this information regarding only *one* of them), are as follows:

1. *Discount on Sales.* A summary posting is made possible, thus saving the posting to the account for each separate item. This advantage not only saves time, but also avoids error due to the well-known fact that when thirty items are posted there are thirty chances of error. The column also acts as a convenient checking device on the accuracy of the two adjoining columns, namely, on Accounts Receivable and on Net Cash columns.

2. *Discount on Purchases.* Exactly the same advantages that have been mentioned regarding Discount on Sales apply to this account.

3. *Expense Column.* Summary posting is made possible, thus avoiding individual postings, thereby saving time and minimizing the chance of error.

(Pp. 42–45); M. & R., 161–168; H., 343–345; S. P., 142–145; D., 36–37.

2. *Do the same for the Journal.*

2. On the debit side Notes Receivable column and Accounts Payable column; on the credit side Notes Payable column. The advantages of the Notes Payable column are exactly those which have been mentioned in connection with the Expense column on the credit side of the Cash Book. In addition to these advantages, we may say on behalf of the Accounts Receivable and of the Accounts Payable columns, that they make possible the keeping of controlling accounts, for it should be recalled that controlling accounts are only practical when special columns in books of original entry are provided. (The advantages of the three columns have been discussed, whereas the student is called upon to give this information, for only *one* of them.)

(Pp. 42–45); M. & R., 161–174; D., 37–38.

3. *What are Controlling Accounts? Describe them, pointing out their advantages.*

3. See answer to Exercise 2, Group One, page 1.

4. *Show that special columns are essential for the use of Controlling Accounts.*

4. Without special columns Controlling Accounts would not exist, because to keep summary accounts in the General Ledger would necessitate the compiling of information regarding the totals to be posted. But if there were no special columns in books of original entry, these totals could be obtained only by a separate tabulation and compilation. The making of this separate tabulation would necessitate extra posting or else arrangement of the items by means of analysis. The only way to avoid this analysis would be to take the totals from the accounts in the separate ledgers, and to post such totals into the summary account of the General Ledger. But in this case errors which were made in

the subsidiary Ledger would be duplicated in the General Ledger, and the check provided by real Controlling Accounts, would be absent.

(P. 31); C., 54, 55, 59, 61; M. & R., 161; E., 124–127.

5. *For what items do we employ the Journal in advanced bookkeeping? Why is this so?*

5. The Journal is employed, in advanced bookkeeping, only for such original entries as have not had provided for them special books of original entry. Thus sales and purchases and cash items are *not* entered in the Journal. Even returned purchases and returned sales are frequently not entered in the Journal, because "return" books are employed. Hence the Journal is really employed very little during the ordinary routine of a business, but is used for opening and closing entries, and for adjustments. This is so because experience has made clear that maximum efficiency is obtained only through the use of specialized books. Accordingly, specialized books (really specialized journals) have been developed to such a point that very little is left for Journal entries.

H., 343; B., 18–19, 64–65; S. P., 89–92.

Group Two

2. *Enter the following transactions:*

May, 1913.

1. *L. B. Collins began the flour and grain business by investing cash $8,500.00, office furniture $300.00, and merchandise as follows: 1,000 bu. wheat @ $1.00; 850 bbl. potatoes at $2.00; total investment, $11,500.00.*
1. *Paid in cash: Rent, $75.00; printing and stationery, $18.50; office fixtures, $125.00.*
2. *Bot. of L. C. Smith, 2/10, n/30, 2,000 bu. corn @ 60c, $1,200.00.*

2. *Bot. of R. Rogers, 2/10, n/30, 200 bbl. flour @ $7.80, $1,560.00.*
3. *Bot. of R. Brown, on account, 2,000 bu. wheat @ $1.00, $2,000.00.*
4. *Sold R. Thom & Bro., on account, 1,000 bu. corn @ 80c, $800.00.*
4. *Sold M. Mullin & Son, on their 15-day note, 150 bbl. flour @ $10.00, $1,500.00.*
5. *Returned to R. Rogers 10 bbl. flour @ $7.80, on account of poor quality. Received credit for $78.00.*
6. *Discounted my own two-months' note at bank. Face $5,000.00, discount $50.00, net proceeds $4,950.00.*
6. *Paid in cash: Clerk hire, $40.00; tip to janitor, $5.00.*
6. *Drew for private use, cash, $100.00.*
6. *Sold Brown & Robbins, on their 10-day note, 1,000 bu. wheat @ $1.25, $1,250.00.*
6. *Donated to Salvation Army, 1 bbl. flour, $8.00; to Sea Side Home, cash, $5.00. (Charge to Expense Account; credit Sales Account and Cash Account, respectively.)*
8. *Sold Cooper & Co., 2/10, n/30, 600 bbl. potatoes @ $2.25, $1,350.00.*
9. *Sold Thom & Bro., 2/10, n/30, 100 bu. wheat @ $1.25. Sold H. Lee, on acct., 500 bu. wheat @ $1.25.*
10. *Paid L. C. Smith, cash, in full of account of inv. of 5/2 less 2% $1,176.00.*
11. *Bot. of L. C. Smith, 2/10, n/30, 200 bbl. potatoes @ $1.50. Bot. of H. M. Case, on acct., 300 bbl. potatoes @ $1.50.*
12. *Paid R. Rogers, on account, cash, $1,000.00, receiving credit for $1,020.00. (Note.—This is a part payment of the May 2 invoice; 2% of $1,000.00 is $20.00, the credit to Discount on Purchases Account. Mathematically and theoretically, we should have received credit for $1,020.41, $1,000 divided by 98%. The practice varies.)*

13. *Gave R. Rogers my 30-day note for balance of account, $462.00. Sold B. Doe, on acct., 400 bu. wheat @ $1.25.*
13. *Paid clerk hire, cash, $50.00.*
13. *Sent goods home for private use, 2 bbl. flour @ $9.00, $18.00. Bot of H. M. Case, on acct., 500 bbl. potatoes @ $1.50.*
15. *Gave R. Brown my 15-day note, on account, $1,000.00.*
16. *Discounted Mullin's note of 5/4, proceeds $1,499.25.*
17. *Cooper & Co. paid their invoice of 5/8, less 2% cash, $1,323.00.*
19. *Thom & Bro. gave us their 15-day note for invoice of 5/4, less 1%, $792.00. (Charge Notes Rec. Account $792.00, Disc. on Sales Account $8.00; credit R. Thom & Bro. $800.00.)*
20. *Bot. store property for $6,000.00, cash. (Charge Real Estate Account.)*
22. *Paid plumbing bill, cash, $25.00.*
26. *Paid R. Brown in full of account, cash, $1,000.00.*
30. *Paid my note of 5/15, favor of R. Brown, cash, $1,000.00.*
31. *Paid in cash: Clerk hire, $50.00; gas bill, $7.50; telephone bill, $12.00.*

Enter in books of original entry (Sales Book, Purchase Book, special column Cash Book, special column Journal) the review set furnished you herewith. The columns in the Cash Book, debit side, are Accounts Receivable, Discount on Sales, Net, General; on the credit side, Accounts Payable, Discount on Purchases, Net, General.

The Journal contains six columns: Notes Receivable, Accounts Payable, General, on the debit side; on the credit side, General, Accounts Receivable, Notes Payable. The Sales Book contains three money columns: the first for extensions; the second for cash sales; and the third for ordinary sales.

1.

Journal

NOTES REC.	ACCTS. PAY.	GENERAL	L. F.		L. F.	GENERAL	ACCTS. REC.	NOTES PAY.
				MAY 1, 1913				
		8500 00	C.B.1	Cash				
		300 00	5	Fur. & Fix.				
		2700 00	2	Mdse. Inv.				
				To L. B. Collins, Prop.	1	11500 00		
				Investment				
				4				
1500 00			√	Notes Rec.				
				To M. Mullin & Son	1		1500 00	
				15-day note; Inv. of 5/4				
				5				
	78 00		1	R. Rogers				
				To Mdse. Purchases	5	78 00		
				Ret. 10 bbls. flour (poor quality)				
				6				
1250 00			√	Notes Rec.				
				To Brown & Robbins	2		1250 00	
				10-day note; Inv. of 5/6				
		8 00	4	Expense				
				To Mdse. Sales	3	8 00		
				Donated 1 bbl. flour to Salvation Army				
				13				
	462 00		1	R. Rogers				
				To Notes Payable	√			462 00
				My 30-day note for balance of account				

Journal—(*Continued*)

NOTES REC.	ACCTS. PAY.	GENERAL	L. F.		L. F.	GENERAL	ACCTS. REC.	NOTES PAY.
				MAY 13, 1913				
		18 00	1	L. B. Collins, Prop.				
				To Mdse. Sales	3	18 00		
				For private use				
				15				
	1000 00		2	R. Brown				1000 00
				To Notes Pay.	√			
				My 15-day note on acct.				
				19				
792 00			√	Notes Rec.				
		8 00	8	Dis. on Sales				
				To Thom & Bros.	3		800 00	
				Rec'd their 15-day note for Inv. of 5/4 less 1%				
				21				
		1500 00	10	Notes Rec. Discounted				
				To Notes Rec.	9	1500 00		
				Contingent liability on Mullin's note of 5/4, extinguished				
				31				
3542 00		3542 00	9	Notes Rec., Dr., total				
	1540 00	1540 00	7	Accts. Pay., Dr., total				
				To Accts. Rec., Cr., total	6	3550 00	3550 00	
				Notes Pay., Cr., total	12	1462 00		1462 00
		18116 00				18116 00		

Cash Book

CASH RECEIPTS

DATE		L. F.			ACCTS. REC.	DIS. ON SALES	NET	GENERAL
	1913							
May	1	J. 1	L. B. Collins, Prop.	Investment				8500 00
	6	12	Notes Pay.	Dis. my 2-mos. note				5000 00
	16	10	Notes Rec. Discounted	Dis. Mullin's note of 5/4				1500 00
	17	5	Cooper & Co.	Inv. of 5/8 less 2%	1350 00	27 00	1323 00	
		6	Accts. Rec.	Cr.	1350 00			
31		8	Dis. on Sales	Dr.		27 00		
							1323 00	1323 00
		13	Cash Receipts for mo.	Dr.				16323 00
								16323 00

Cash Book

CASH DISBURSEMENTS

DATE		L. F.			ACCTS. PAY.	DIS. ON PUR.	NET	GENERAL
1913								
May	1	4	Expense	Rent, $75; Stationery, $18.50				93.50
		5	Fur. & Fix.					125.00
	6	18	Dis. on Notes	My 2-mos. note				50.00
		4	Expense	Clerk hire, $40; Tip to Janitor, $5				45.00
		1	L. B. Collins, Prop.	Private use				100.00
		4	Expense	S. S. home				5.00
	10	5	L. C. Smith	5/2, less 2%	1200.00	24.00	1176.00	
	12	1	R. Rogers	On a/c, less 2%	1020.00	20.00	1000.00	
	13	4	Expense	Clerk hire				50.00
	16	18	Dis. on Notes	Mullin's				.75
	20	17	Real Estate	Store prop.				6000.00
	22	4	Expense	Plumbing				25.00
	26	2	R. Brown	In full	1000.00		1000.00	
	30	12	Notes Pay.	R. Brown, 5/15				1000.00
	31	4	Expense	Clerk hire, $50; Gas, $7.50; Telephone, $12				69.50
		7	Accts. Pay.	Dr.	3220.00			
		8	Dis. on Purchases	Cr.		44.00		
							3176.00	3176.00
		14	Cash Disbursements for month	Cr.				10739.75
			*Balance					5583.25
								16323.00

*Red Ink.

Purchase Book

1913				L. F.	UNIT PRICE	EXTENSION	TOTAL
May	2	L. C. Smith, 2/10 n/30	2000 bu. Corn	5	.60	1,200.00	1,200.00
	2	R. Rogers, 2/10 n/30	200 bbls. Flour	1	7.80	1,560.00	1,560.00
	3	R. Brown, on a/c	2000 bu. Wheat	2	1.00	2,000.00	2,000.00
	11	L. C. Smith, 2/10 n/30	200 bbls. Potatoes	5	1.50	300.00	300.00
	11	H. M. Case, on a/c	300 bbls. Potatoes	6	1.50	450.00	450.00
	13	H. M. Case, on a/c	500 bbls. Potatoes	6	1.50	750.00	750.00
	31	Mdse. Pur., debit, total purchases of Mdse. for month		5			6,260.00
	31	Accts. Pay., credit, total purchases of Mdse. for month		7			6,260.00

Sales Book

1913				L. F.	UNIT	EXTENSION	CASH SALES	TIME SALES
May	4	R. Thom & Bro., on a/c	1000 bu. Corn	3	.80	800.00		800.00
	4	M. Mullin & Son, note	150 bbls. Flour	1	10.00	1,500.00		1,500.00
	6	Brown & Robbins, note	1000 bu. Wheat	2	1.25	1,250.00		1,250.00
	8	Cooper & Co., 2/10 n/30	600 bbls. Potatoes	5	2.25	1,350.00		1,350.00
	9	Thom & Bro., 2/10 n/30	100 bu. Wheat	3	1.25	125.00		125.00
	9	H. Lee, on a/c	500 bu. Wheat	6	1.25	625.00		625.00
	13	B. Doe, on a/c	400 bu. Wheat	7	1.25	500.00		500.00
	31	Mdse. Sales, credit, total sales for month		3				6,150.00
	31	Accts. Rec., debit, total sales for month		6				6,150.00

2. *Post to the three Ledgers (General, Customers', and Creditors'), keeping them apart from each other. If loose Ledger sheets are employed, make sure that no sheet contains accounts belonging to another Ledger. Allow five lines each, in the General Ledger, for Accts. Rec. and Accts. Pay. No Personal Account, except the proprietor's, should be in the General Ledger.*

2. No solution is necessary. The answer to Exercise 3, following, will be sufficient.

3. *Take a Trial Balance of the General Ledger. Prepare schedules of the Sales Ledger and of the Purchase Ledger.*

3.

Trial Balance

May 31, 1913

L. B. Collins, Proprietor (or Capital)		$11,382.00
Real Estate	$6,000.00	
Mdse. Inventory	2,700.00	
Mdse. Purchases	6,182.00	
Furniture and Fixtures	425.00	
Interest and Discount	50.75	
Notes Payable		5,462.00
Notes Receivable	2,042.00	
Expense	296.00	
Accounts Receivable	1,250.00	
Accounts Payable		1,500.00
Discount on Sales	35.00	
Discounts on Purchases		44.00
Mdse. Sales		6,176.00
Cash	5,583.25	
	$24,564.00	$24,564.00

Schedule of Customers' Balances in Sales Ledger:

H. Lee	$625.00
B. Doe	500.00
R. Thom & Bro.	125.00
Total	$1,250.00

Schedule of Creditors' Balances in Purchase Ledger:

H. M. Case	$1,200.00
L. C. Smith	300.00
Total	$1,500.00

4. *If you wish to do so, prepare the statements and close the books.**

4 (*a*) **Statement of Assets and Liabilities of L. B. Collins**

MAY 31, 1913

Cash	$5,583.25	Accounts Payable	$1,500.00
Notes Receivable	2,042.00	Notes Payable	5,462.00
Accounts Receivable	1,250.00		
Furniture and Fixtures	382.50	L. B. Collins, Prop.,	
Real Estate	6,000.00	*Net Capital*	12,059.35
Mdse. Inv. 5/31/13	3,763.60		
	$19,021.35		$19,021.35

*(Mdse. Inventory, $3,763.60; 10% depreciation on furniture and fixtures.)

(*b*) **Profit and Loss Statement**

MAY 31, 1913

Sales:	$6,176.00	
Less Dis. on Sales	35.00	
NET SALES		$6,141.00
Mdse. Inv. 5/1/13	2,700.00	
Purchases	6,182.00	
	8,882.00	
Less Inv. 5/31/13	3,763.60	
Cost of Goods Sold		5,118.40
GROSS PROFIT ON SALES		$1,022.60
Expenses:		
Bank Dis.	$50.75	
Office Expense	156.00	
Office Salaries	140.00	
Office Furniture Depreciation	42.50	
	389.25	
Less Dis. on Purchases	44.00	
		345.25
Net Profit		$677.35

(*Proof:*
Proprietor's net investment..............$11,382.00
Net profit.............................. 677.35
Net Capital....................$12,059.35)

SOLUTIONS TO EXERCISES

CHAPTER IV

SINGLE ENTRY VERSUS DOUBLE ENTRY

Group One

1. *Differentiate between Single Entry and Double Entry Bookkeeping.*

1. Single Entry Bookkeeping keeps so-called Personal Accounts only; Double Entry Bookkeeping keeps, in addition, so-called Real and Nominal Accounts. The accuracy of posting in Double Entry is proved by means of a Trial Balance; the less known and more cumbersome Proof of Posting is the corresponding device in Single Entry. Whereas the progress and condition can be obtained from both kinds of bookkeeping, this information when obtained from Double Entry books is far more reliable, and moreover, checking devices are available in the Double Entry system. But much more important still, not only can profits or losses be determined in Double Entry, as in Single Entry, but in the former system the *sources* of such profits are available. The importance of this item must not be overlooked. In addition, Double Entry provides the means of preparing statistical information of great value, and because of the checks which it affords, acts as a deterrent upon crime.

(Pp. 78–79, 81–82); M. & R., 17–18; C, 313–314; G., II, 205–206; M. B., Appendix A; E., 54–55, 58–59.

2. *Mention three important items of information which could not be obtained from a Single Entry set, but which could be gotten from a Double Entry set.*

2. (*a*) Cost of manufacturing.
   (*b*) ~~The department which is most profitable.~~
   (*c*) What per cent. of total sales is represented by the amount paid for salaries during the year.
   (Any three items which deal with Nominal Accounts or statistical items would be equally correct.)

(Same references as for Exercise 1, above.)

3. *Write a letter to the proprietor of a wholesale dry-goods house whose books have been kept by Single Entry so as to convince him that he should have them changed to Double Entry.*

3. Each letter should refer to the advantages of Double Entry over Single Entry, and should, moreover, show the application of these advantages to the specific problems of the individual concern involved. The advantages have already been enumerated in answers to Exercises 1, 2 and 4 of Group One, and in the summary on pages 81-82 of Elements of Accounting. The examples of the specific references to the books of a wholesale dry-goods house are herewith given:

(*a*) The profits on domestic laces could be separated from the profits on the imported laces.
(*b*) The yearly cost of advertising could readily be ascertained.
(*c*) Information as to the progress of each department could readily be ascertained, etc., etc.

4. *Argue in favor of Double Entry for a retail furniture concern.*

4. A considerable number of accountants believe that Single Entry is as practical as Double Entry for retail concerns. That this is not so, and especially not so for retail furniture stores, is about to be made clear. Though it is true that most importance should attach to the number of accounts with customers which must be kept, it is nevertheless true that the inconsiderable num-

ber of Nominal Accounts, which would serve a very useful purpose, could be kept without material increase in cost. This would be so due to the well-known device of special columns in books of original entry, and when it is considered that the amount of work necessary for the proper maintaining of the Customers' Ledger necessitates the employment of a bookkeeper with a sufficient knowledge to handle a modern Double Entry set, and when it is recollected, moreover, that practically no additional cost would be incurred by the keeping of the very important Nominal Accounts, it seems that the argument should be in favor of Double Entry books rather than in favor of Single Entry books.

The burden of proof lies with him who defends Single Entry.

N. C., 151–181; E., 67–68.

5. *How would you change a Double Entry set to a Single Entry one?*

5. This proposition is a theoretical one and does not, as a general rule, appear in actual practice. The theory upon which it is based is a simple one: the elimination from the Ledger of all except Personal Accounts. The accounts which will then remain are those which constitute a Single Entry Ledger.

6. *Outline a form for the "Proof of Posting" for a Single Entry Ledger to which postings are made from a Journal, Cash Book, Sales Book, and Purchase Book.*

(Solution on page 23.)

7. *State how you can ascertain the profit or loss of a business whose books have been kept by Single Entry.*

7. The only way of ascertaining the profit or loss of a concern whose books have been kept by Single Entry is to get the difference between the present capital, as shown by a Statement of Assets and Liabilities, and the net investment of the concern.

(Pp. 71–72); M. & R., 14; K., 17, 19; D., 19–20; E., 67.

6. (Question on page 22.) **Proof of Posting**

	Debits	Credits
Journal, page 1	$2,150 00	$3,000 00
page 2	2,650 00	4,750 00
page 3	4,875 00	1,950 00
Cash Book, posting column:		
debit side		4,321 00
credit side	2,680 00	
Sales Book	5,650 00	
Purchase Book		2,500 00
	$18,005 00	$16,521 00

(Pp. 70–71); K., 18.

8. *Describe card Ledgers and loose-leaf systems.*

8. Card Ledgers are Ledger forms printed upon cardboard. The rulings may be the same as the regular form of Ledger, or they may be modified to suit specific conditions. The advantages usually mentioned on behalf of such cards are the following:

(*a*) They are self-indexing.
(*b*) They are easily accessible.
(*c*) They minimize errors in posting.
(*d*) They improve office efficiency.
(*e*) "Dead" cards, that is, cards with people with whom we no longer deal, are filed away so as not to interfere with "live" accounts.

The disadvantages attributed are principally:

(*a*) They may be lost.
(*b*) They may be misplaced.

Loose-leaf systems are practically bound Ledgers with replaceable leaves. Almost all of the advantages of card ledgers are attributed to loose-leaf systems, but it is claimed for them that the disadvantages of the card system have been eliminated.

(Pp. 79–81); H., 348–350; M., 309–311, 507; N. C., 158–160.

Group Two

1. *L. E. Smythe began business on April 1, 1912, by investing cash, $3,000.00; merchandise, $1,700.00; and office furniture, $400.00. His withdrawals were as follows: July 3, 1912, cash, $100.00; Dec. 27, 1912, cash, $250.00; Feb. 5, 1913, merchandise for private use, $30.00. On March 31, 1913, his Ledger contains his own account and also the following balances:*

(a) Customers:		
	Bailey & Co.	*$495.00*
	R. Sommers	*1,365.00*
	Jansen & Rowe	*2,400.00*
	T. L. Sellers	*590.00*
(b) Creditors:		
	Cole & Johnson	*$1,500.00*
	Allis & Co.	*490.00*

From other sources of information it is ascertained that the cash in bank amounts to $6,415.00, and that there is $165.00 in the safe. The goods are inventoried at $3,400.00; office furniture, $300.00; Mr. Smythe holds a note in his favor for $200.00; while he has outstanding two notes of $4,000.00 each, both in favor of his bank.

(a) Find the present value of Mr. Smythe's business, March 31, 1913.

(b) Find his net profit or net loss.

1 (*a*). **Statement of Assets and Liabilities of L. E. Smythe**

MARCH 31, 1913

ASSETS		LIABILITIES	
Cash (in bank)	$6,415.00	Accounts Payable	$1,990.00
Cash (in safe)	165.00	Notes Payable	8,000.00
Mdse. Inventory	3,400.00		
Accounts Receivable	4,850.00	*Total Liabilities*	$9,990.00
Notes Receivable	200.00	L. E. Smythe, Net Capital	5,340.00
Office Furniture	300.00		
	$15,330.00		$15,330.00

(b)

Statement of L. E. Smythe's Profit

FOR THE YEAR ENDED MARCH 31, 1913

Net Capital, as per Statement of Assets and Liabilities, March 31, 1913	$5,340.00
Net Investment, as per Ledger	4,720.00
Net Profit	$620.00

(Pp. 71–72, 74); K., 21; G., I, 7–8.

2. *Change the old books to the Double Entry system.*

2 (a) Entry in old Journal:

MARCH 31, 1913

L. E. Smythe, Prop., Cr. $620.00

To credit Mr. Smythe's a/c with the net profit for the first year as per Statement of Profit.

(This entry should be made whether books are to be changed to double entry or not.)

(b)

	MARCH 31, 1913 I have this day decided to change my books from Single Entry to Double Entry. The following items constitute a true exhibit of my condition to-day:				
3	Cash	6,580	00		
5	Mdse. Inventory	3,400	00		
√	Bailey & Co.	495	00		
√	R. Sommers	1,365	00		
√	Jansen & Rowe	2,400	00		
√	T. L. Sellers	590	00		
10	Notes Receivable	200	00		
12	Office Furniture	300	00		
11	To Notes Payable			8,000	00
√	Cole & Johnson			1,500	00
√	Allis & Co.			490	00
√	L. E. Smythe, Prop.			5,340	00
	All of the above items have been posted as indicated. The items checked were already in the Ledger.				

(Pp. 72–76); K., 19–20; G. A., 122–124.

3. *Close the old books and open a new set to be kept by Double Entry.*

3 (*a*) Entry to close the old books, in the *old* Journal:

	March 31, 1913					
	I have this day decided to change my books to Double Entry. The following entry is for the purpose of closing all the accounts in the old Ledger as a necessary preliminary.					
1	L. E. Smythe, Prop.	Dr.			5,340	00
7	Allis & Co.	Dr.			490	00
7	Cole & Johnson	Dr.			1,500	00
8	Bailey & Co.	Cr.			495	00
8	R. Sommers	Cr.			1,365	00
9	Jansen & Rowe	Cr.			2,400	00
9	T. L. Seller	Cr.			590	00

(*b*) Entry to open the new books in the *new* Journal:

	April 1, 1913				
	I have this day decided to open a new set of double entry books. The following items constitute my true condition to-day:				
3	Cash	6,580	00		
5	Mdse. Inventory	3,400	00		
6	Bailey & Co.	495	00		
7	R. Sommers	1,365	00		
8	Jansen & Rowe	2,400	00		
9	T. L. Sellers	590	00		
10	Notes Receivable	200	00		
12	Office Furniture	300	00		
11	To Notes Payable			8,000	00
13	Cole & Johnson			1,500	00
14	Allis & Co.			490	00
15	L. E. Smythe, Prop.			5,340	00
	All of the above items have been posted as indicated.				

(Pp. 76–77); K., 20–21.

4. (Question on page 29.)

NOTES REC.	ACCTS. PAY.	GENERAL	L. F.	APRIL 1, 1913		L. F.	GENERAL	ACCTS. REC.	NOTES PAY.
				I have this day decided to open a new set of double entry books. The following items constitute my true condition to-day.					
		6,580 00	3	Cash					
		3,400 00	5	Mdse. Inventory					
		4,850 00	6	Accts. Rec.					
			1	Bailey & Co.	495.				
			2	R. Sommers	1,365.				
			3	Jansen & Rowe	2,400.				
			4	T. L. Sellers	590.				
		200 00	10	Notes Rec.					
		300 00	12	Office Furniture					
				To Notes Pay.		11	8,000 00		
				Accts. Pay.		7	1,990 00		
				Cole & Johnson	1,500.	1			
				Allis & Co.	490.	2			
				L. E. Smythe, Prop.		15	5,340 00		

(NOTE: Individual debtors and creditors have been posted to Sales Ledger and Purchase Ledger, respectively.)

(Pp. 77–78.)

6. (Question on page 29.) L. E. SMYTHE, PROPRIETOR

19	12					19	12					
July	3	Cash	C.B. 2	100	00	Apr.	1	Investment	J. 1	5,100	00
Dec.	27	Cash	C.B.12	250	00	19	13				
19	13					Mch.	31	Net Profit	11	620	00
Feb.	5	Mdse.	J. 7	30	00						
Mch.	31	*Net Capital**		5,340	00						
				5,720	00					5,720	00
						19	13				
						Apr.	1	Balance		5,340	00

*Red.

4. *Open the new books, introducing customers' and creditors' Controlling Accounts. (Assume that the old books have been closed as in 3 (a), page 26.)*

(Solution on page 27.)

5. *Make the last Single Entry Journal entry in Mr. Smythe's books.*

5.

MARCH 31, 1913

L. E. Smythe, Prop., Cr. $620.00

To credit Mr. Smythe's account with the net profit for the first year, as per Statement of Profit.

(This Journal entry should be made whether books are to be changed to double entry or not.)

(P. 74.)

6. *Show Mr. Smythe's account in the old Ledger after posting the entry referred to in the last question.*

(Solution on page 28.)

SOLUTION TO EXERCISES

CHAPTER V

PARTNERSHIP ACCOUNTING

1. *State the six most essential points in a copartnership agreement.*

Group One

1. Besides the perfunctory ones such as date, names of parties, etc., the following are the six most essential points:
   (*a*) Rights and duties of the partners.
   (*b*) Division of profits and losses.
   (*c*) Compensation of partners.
   (*d*) Limitation on drawings.
   (*e*) Interest on investments.
   (*f*) The procedure in case of death or dissolution.

(Pp. 88–89); H. L., 247–250; G. L., 229–234; M., 41–44; G. A., 147–149; D., 52–53.

2. *How are profits divided between partners?*
2. Equally, except in the case where a specific agreement is made to the contrary. In case such specific agreements are entered into, profits are then divided as stipulated. Common divisions are in fixed ratios as $\frac{1}{3}$ and $\frac{2}{3}$; $\frac{3}{4}$ and $\frac{1}{4}$; $\frac{3}{8}$ and $\frac{5}{8}$; and in proportion to original investment, net investment or average investment.

(Pp. 93–94); G. A., 173–176.

3. *Mention one legal and one accounting step necessary in case of the death of a partner.*

3. No legal step is prescribed by statute, not even the customary notice necessary in case of ordinary dissolution. One of the accounting steps which is essential is to close the books for the purpose of ascertaining the interest of the deceased partner in the business at the time of death, unless the articles of copartnership specified a different procedure.

H. L., 251; G. L., 176, 240; D., 105.

4. *Analyze and discuss the following clause, taken from a certain partnership agreement:*

> *"VIII. And it is further agreed that the said party of the second part is to pay to the said party of the first part the sum of three thousand dollars ($3,000.00); for which the said party of the second part shall receive a one-third (1-3) interest in the said business of the said party of the first part. . . ."*

4. This clause is presented because of the ambiguity which is frequently met with in practice, in similar situations. The intention of the partners, to judge by Clause VIII referred to, is that the incoming partner is to pay $3,000 *personally* to the original partner, in return for which the original partner is to transfer one-third of his existing capital to the said incoming partner. This seems to be the plain intent of the clause, but it is just possible, and in practice it is quite probable, that the incoming partner thought he was to contribute $3,000 to the new firm's capital, for which he was to receive a one-third interest in the joint capital thus created. The suggestion of the accountant should be that the parties at issue should clearly arrive at a mutual understanding of just what they wish to do and then to set it down in language unmistakable and unambiguous.

(Pp. 105–106); M., 41.

5. *Define investment, net investment, average investment, Drawing Account, interest on investment.*

5. Definitions: (Every definition should consist not only of the definition as ordinarily understood, but in addition, if possible, it should be supplemented by an illustration.)

(*a*) *Investment.* The investment has reference to the amount contributed by a proprietor, whether individual or partner, to his concern. It is a very general term and is likely to be misunderstood. It may refer to his original investment or to his net investment, and, in some cases, even to his average investment. As an illustration, Mr. Doe's investment (page 95 of Elements of Accounting) was $6,000.00. His net investment, as will be explained in (*b*) below, was $5,800.00.

(*b*) *Net Investment.* The net investment represents the difference between the original investment, or the investment at the beginning of a period, and the total of withdrawals during the period. However, if there have been additional investments besides the original or first-of-the-period investment, then such additions are to be taken into consideration before determining the amount of the net investment. In the case of John Doe (page 95 of Elements of Accounting), the net investment was $6,000.00 plus $150.00 less $350.00, or $5,800.00.

(*c*) *Average Investment.* The average investment is an amount somewhere between the maximum and the minimum investments for the period under review. It is found by taking into consideration the *time* during which the investment was at the service of the business. In the case of Mr. Doe (pages 95-96), it was a few cents more than $6,008.00.

(*d*) *Drawing Account.* The Drawing Account is the name given to that portion of a partner's interest in the business which is not shown in his capital account. To this Drawing Account are carried the withdrawals of money during the current period, as also any additions which arise in consequence of routine and unusual items, accruing to the partner's credit. The net profit or

loss for the period is also carried to this account, at which time the balance is adjusted either by a transfer to the Capital Account, or by permitting the balance to remain for the next period, depending upon agreement between the partners. A synonym for Drawing Account is Personal Account or Private Account. An illustration of this account will be found on page 95 of Elements of Accounting (John Doe, Personal).

Some untrained bookkeepers regard the Drawing Account as synonymous with Partners' Salary Account. That this is not the case should hardly require emphasis.

(*e*) *Interest on Investment.* By interest on investment is meant an allowance of interest, *always by agreement,* on the investments of the partners. The rate of interest is subject to agreement, as well as the amount upon which it is to be based.

It sometimes refers to the interest which stocks and bonds, owned by the business, have earned.

Group Two

1. *The net profit of the firm of A., B., and C. was found to be $6,000.00. The net investment of the firm was $80,000.00, divided as follows: A., $40,000.00; B., $25,000.00; C., $15,000.00. Show Journal entry to apportion the net profit.*

1.	Profit and Loss	$6,000.00	
	To A, Drawing %		2,000.00
	B, Drawing %		2,000.00
	C, Drawing %		2,000.00

(In the absence of a specific agreement to the contrary, remember that profits are divided equally between partners.)

(P. 93.)

2. *D. and E. are partners. Part of D.'s original investment consisted of ten shares of Old Jersey Bridge Co. stock, guaranteed by him to be worth $60.00 per share, and accepted and entered at this figure. At the end of the year the stock was disposed of at $18.00 per share. Make the necessary entries.*

2. (At the time of the formation of the partnership, an entry was made, debiting, among the other assets, Old Jersey Bridge Company Stock for $600.00, while the credit to D's capital account included this amount.)

Cash	$180.00	
D's Drawing %	420.00	
To Old Jersey Bridge Company Stock		$600.00

(Instead of charging D's Drawing Account, some accountants would prefer to charge his Capital Account. Do as you please in the matter.)

3. *Find Richard Roe's average investment.* (*See page 95.*)

3. RICHARD ROE

50 x 9	$450.00	4000 x 12	$48,000.00
50 x 8	400.00		1,300.00
100 x 4	400.00		
50 x 1	50.00		12 | 46,700.00
	$1,300.00	Average investment	$3,891.67

(Pp. 95–96).

4. *Show the Journal entry to apportion the profit of $1,000.00 between Doe and Roe (see page 95) in case it is provided that:*

(*a*) *Profits are to be shared equally.*

(*b*) *Profits are to be shared in proportion to average investments.*

4. (*a*)	Profit and Loss	$1,000.00	
	To John Doe, Drawing		$500.00
	Richard Roe, Drawing		500.00
(*b*)	Profit and Loss	1,000.00	
	To John Doe, Personal		606.89
	Richard Roe, Personal		393.11

$$\frac{6008}{9899.67} \text{ x } \$1000. = \$606.89$$

$$\frac{3891.67}{9899.67} \text{ x } \$1000. = \$393.11$$

(Pp. 93–96.)

5. *Suggest some arrangement between Doe, Roe, and Soe (see page 97) to avoid even the last Journal entry shown. (The object of this question is to test the student's ability to get at the basic meaning of accounting solutions.)*

5. Roe might pay Doe $5.00 and Soe might pay Doe $10.00.

(Pp. 97–98.)

6. *To how much interest is Richard Roe entitled at six per cent. per annum? (See page 95.)*

6. The solution to Exercise 3, Group Two, above, shows that Richard Roe's investment was equivalent to an investment of $46,700.00 for one month. ½% (1/12 of 6%) of $46,700.00 is $233.50, the required interest.

(Pp. 98–99.)

7. *You are requested to determine the good will of a concern from whose books you gather the following facts:*

Net investments during 1908, $16,000.00; 1909, $18,-

500.00; 1910, $20,000.00; 1911, $20,000.00. The net profits during the same period were: 1908, $2,900.00; 1909, $3,100.00; 1910, $4,000.00; 1911, $2,600.00. You also find that no interest had been allowed on Capital Accounts, and that fair depreciation on fixtures and proper deductions for bad debts had been made.

7 (*a*)

Working Sheet

YEARS	INVESTMENTS	NET PROFITS	INTEREST ON INVESTMENT @ 6%	EXCESS PROFITS
1908	$16,000.00	$2,900.00	$960.00	$1,940.00
1909	18,500.00	3,100.00	1,110.00	1,990.00
1910	20,000.00	4,000.00	1,200.00	2,800.00
1911	20,000.00	2,600.00	1,200.00	1,400.00
				4|$8,130.00
	AVERAGE YEARLY EXCESS PROFITS			$2,032.50

(*b*) The above analysis discloses the fact that the average excess profits per year amounted to $2,032.50. The experience of accountants is that in paying for good will, from two to five years' purchase of the excess profits is a usual payment. The actual purchase price must be determined between the buyer and the seller, but on the basis of experience it is suggested that from two to four times $2,032.50, or from $4,065.00 to $8,130.00, be the amount allowed for good will.

(Caution: This statement is made despite the fact that during the last year, 1911, there occurred a falling off in net profits from $4,000.00 to $2,600.00. This decline in profits must be explained before anything should be allowed for good will. If the decline is likely to continue, or if it cannot be explained away on logical grounds, then the question arises whether there is the likelihood of profits continuing upon change of proprietorship. If the answer is in the negative, the report made above would be modified accordingly.)

(Pp. 103–105); M., 131–135; G. I., 15, 166–167.

8. *F. and G. are partners in a wholesale dry-goods business. F., the senior partner, agrees to retire, accepting for his interest $8,000.00 cash and five notes of $2,000.00 each, without interest, maturing at two-month intervals, commencing six months hence. The following Balance Sheet is prepared prior to paying F. off:*

Balance Sheet of F. & G.

DECEMBER 31, 1914

ASSETS		LIABILITIES AND CAPITAL	
Cash	$12,000.00	Notes Payable	$15,500.00
Notes Receivable	10,000.00	Accounts Payable	11,000.00
Accounts Receivable	24,000.00		
Merchandise	10,000.00	Total Liabilities	$26,500.00
Fixtures	2,500.00		
		F., Capital	17,000.00
		G., Capital	15,000.00
	$58,500.00		$58,500.00

Required, the entry or entries when paying F. off.

8 (*a*)

Good will	$1,000.00	
To F, Capital		$1,000.00

(*b*)

F, Capital	18,000.00	
To Cash		8,000.00
Notes Payable		2,000.00
Notes Payable		2,000.00
Notes Payable		2,000.00
Notes Payable		2,000.00
Notes Payable		2,000.00

(P. 102.)

9. *Prepare a form of dissolution notice in the above premises. (See advertisements in the daily papers.)*

9. DISSOLUTION NOTICE

STATE OF NEW YORK, CITY OF NEW YORK, SS:

I, G, of the City of New York, successor and assignee of all the assets and good will of F and G, heretofore conducting business within this State for more than three years, do hereby certify that I intend to continue conducting or transacting said business under the name of F and G, at 32 Water Street, Borough of Manhattan, in the City of New York, State aforesaid, and that the true or real name of the person conducting or transacting the same is as follows:

Name..................

P. O. Address
32 Water Street
New York City

STATE OF NEW YORK, CITY OF NEW YORK, COUNTY OF NEW YORK, SS:

On this 31st day of December, 1913, before me personally appeared G, to me known and known to me to be the individual described in and who executed the foregoing certificate, and he thereupon acknowledged to me that he executed the same.

.................,
Commissioner of Deeds, City of New York.

(See *Legal Notices* in newspapers.)

10. *Show the Balance Sheet after posting solution for Exercise 8.*

10

Balance Sheet of F. & G.

December 31, 1913

Assets		Liabilities and Capital	
Cash	$4,000.00	Notes Payable	$25,500.00
Notes Receivable	10,000.00	Accounts Payable	11,000.00
Accounts Receivable	24,000.00		
Merchandise	10,000.00	Total Liabilities	$36,500.00
Fixtures	2,500.00		
Goodwill	1,000.00	G, Capital a/c	15,000.00
	$51,500.00		$51,500.00

11. *Make Journal entry if H. pays $20,000.00 cash to the business and receives therefor a one-half interest in it. (After F. has retired.)*

11

(*a*) Goodwill *	$5,000.00	
To G, Capital a/c		$5,000.00
(*b*) Cash	20,000.00	
To H, Capital a/c		20,000.00

(P. 106.)

12. *Entry if he pays G $7,000.00 personally for a one-half interest.*

12

G, Capital a/c *	7,500.00	
To H, Capital a/c		7,500.00

(P. 105-106.)

13. *Entry if he invests $20,000.00 in the business, receiving a proportionate share in it.*

13

Cash	20,000.00	
To H, Capital a/c		20,000.00

(P. 105.)

*"A one-half interest" does not always signify fifty per cent. of the capital investment; it may mean a fifty per cent. sharing of profits alone.

14. *Entry for Exercise 11 if payment was only $12,000.00. Show resulting Balance Sheet.*

14

(a) Cash	12,000.00	
To H, Capital a/c		12,000.00
(b) G, Capital a/c	1,500.00	
To H, Capital a/c		1,500.00

Balance Sheet of G. & H.

Assets		Liabilities and Capital	
Cash	$16,000.00	Notes Payable	$25,500.00
Notes Receivable	10,000.00	Accounts Payable	11,000.00
Accounts Receivable	24,000.00		
Merchandise	10,000.00	Total Liabilities	$36,500.00
Fixtures	2,500.00		
Good will	1,000.00	G., Capital a/c	13,500.00
		H., Capital a/c	13,500.00
	$63,500.00		$63,500.00

(P. 107.)

15. *If in Exercise 1, Group Two, page 24, Mr. Smythe admitted James Franke to a one-third interest in the business upon the investment by the latter of $2,000.00, one-half cash and one-half by a six months' note, with interest at five per cent., show the entries to open a new set of books, employing Controlling Accounts.*

(Solution on page 42.)

16. *L. and M. are partners sharing losses and gains equally. Their books show a credit balance in L.'s account of $6,000.00 and in M.'s of $2,000.00. Their assets amount to $5,000.00, and their liabilities to $2,500.00. What is the financial relationship between the partners after paying the liabilities?*

16. It is evident that if the assets amount to only $5,000.00, while the liabilities amount to $2,500.00, that upon the payment of the liabilities but $2,500.00 will remain for division

among the partners. Inasmuch as their joint capital is $8,000.00 ($6,000.00 plus $2,000.00) there must have been a loss of $5,500.00 ($8,000.00 less $2,500.00). In the absence of a specific agreement to the contrary, we know that profits and losses are to be shared equally between partners. Hence, the loss of $5,500.00 is to be borne equally by Messrs. L and M. Accordingly, each is to be charged with a loss of $2,750.00. The capital accounts of the two partners upon posting this loss follow:

L, Capital

½ Net Loss	$2,750.00		$6,000.00

M, Capital

½ Net Loss	$2,750.00		$2,000.00

An inspection of the foregoing accounts reveals the fact that L is entitled to $3,250.00, whereas M has already (practically) overdrawn his account by $750.00. Therefore, the $2,500.00 of assets which still remain should be given to Mr. L, who would then still be entitled to $750.00. This is just the amount which Mr. M owes to the concern, and he must pay it to Mr. L. A specific answer to the question is, therefore, that upon the payment of the liabilities Mr. L is to receive the balance of assets, $2,500.00, and that then Mr. M still owes to Mr. L the sum of $750.00.

(G. I., 90–91, 185.)

15. (Question on page 40.)

Accts. Pay.	General	L. F.		L. F.	General	Accts. Rec.
			L. E. Smythe and James Franke have this day formed a copartnership under the firm name of ————. The investments of each partner are shown in the following entries:			
			Investment by Mr. Smythe:			
	$8,580.00		Cash			
	3,400.00		Mdse. Inv.			
	4,850.00		Accts. Rec.			
			Bailey & Co. $495.00			
			R. Sommers 1,365.00			
			Jansen & Rowe 2,400.00			
			T. L. Sellers 590.00			
	200.00		Notes Rec.			
	300.00		Office Furniture			
			To Accts. Pay.		$1,990.00	
			Cole & J. 1,500.00			
			Allis & Co. 490.00			
			Notes Pay.		8,000.00	
			L. E. Smythe, Cap.		5,340.00	
			Mr. Franke's Investment:			
	1,000.00		Cash			
	1,000.00		Notes Rec. (6 mo.)			
			To James Franke, Cap.		2,000.00	
	446.66		L. E. Smythe, Cap.			
			To James Franke, Cap.		446.66	
			Transfer from Mr. Smythe's to Mr. Franke's a/c of $446.66, to adjust partnership relations between them, as per agreement.			

(Pp. 46, 54, 105–107.)

SOLUTIONS TO EXERCISES

CHAPTER VI

CORPORATION ACCOUNTING

Group One

1. *What is a corporation?*

1. It is very difficult to define a corporation, so instead of presenting an original one, let us take Chief Justice Marshall's definition:

"A corporation is an artificial being, invisible, intangible, and existing only in contemplation of law. Being the mere creature of law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence. These are such as are supposed best calculated to effect the object for which it was created. Among the most important are immortality, and, if the expression may be allowed, individuality; properties by which a perpetual succession of many persons are considered as the same, and may act as a single individual. They enable a corporation to manage its own affairs, and to hold property without the perplexing intricacies, the hazardous and endless necessity, of perpetual conveyances for the purpose of transmitting it from hand to hand. It is chiefly for the purpose of clothing bodies of men in succession with these qualities and capacities that corporations were invented, and are in use. By these means a perpetual succession of individuals are capable of acting for the promotion of the particular object, like one immortal thing."

(P. 118); H. L., 256; G. L., 247–249; S. L., 211.

2. *Differentiate between common stock and preferred stock.*

2. The stock of a corporation is its capital, that is, the *repre-*

sentation of ownership of the net capital of the corporation. Each share of stock, in general, entitles the owner to one vote for each share held, and to one part of the net assets upon dissolution. The difference between common stock and preferred stock is, essentially, that the preferred stock is given certain rights not possessed by the holders of the common stock. The chief preference is that the preferred stock is entitled to a fixed rate of dividends before the common stock is entitled to any share of the profits. Accordingly, if the profits for a certain year are sufficient to allow a dividend on the preferred stock, say of 5%, but to leave nothing over for the common stockholders, the latter would receive no return on their investment during the period in question. If, however, the business for a certain period did not permit of the "declaring" of the stated dividend on the preferred stock, but the second year's profits were such as to permit the payment of twice the yearly dividend, the holders of the preferred stock would be entitled to only 5%, while the balance would be available for the dividends to the common stockholders. Some preference, however, is such as to provide for the *accumulation* of dividends, and such stock is called "cumulative preferred." Such stock is entitled to the stated dividend each year; if no profits are available during one year the dividend "passed" remains in favor of the preferred stock and is payable before any profits are available for the common stockholders.

Preferences such as privilege of special voting, holding of office, etc., etc., may be granted to the holders of preferred stock, but in all such cases the action is the result of a special agreement expressed in the body of the preferred stock certificate.

(Pp. 118–119); G. L., 264; H. L., 258–259; B. C., 404–417; R. C., 123–128; S. C., 194–199; C. O., 91–104.

3. *What is the relation between the Capital Stock Account of the General Ledger and the Stockholders' Ledger or Stock Ledger?*

3. The Capital Stock Account of the General Ledger may be regarded as a controlling accounting of the Stock Ledger. If the total capitalization of, say, $100,000.00 has been subscribed and issued, then there will be found in the Stock Ledger the accounts of the stockholders aggregating 1,000 shares (par value $100). If all the stock has not been issued, however, then the difference between the Capital Stock Account of the General Ledger and the account which shows the unissued stock, also in the General Ledger, would be the controlling balance for the sum of all the balances in the Stock Ledger.

(P. 120.)

4. *Differentiate between Unsubscribed Stock, Unissued Stock, and Treasury Stock.*

4. Unsubscribed Stock and Unissued Stock are frequently synonymous terms. In Elements of Accounting, Unsubscribed Stock is employed, while Professor Hatfield favors Unissued Stock. If any distinction exists between the two terms it lies in the fact that *some* subscribed stock may not yet have been issued (physically), while *all* unsubscribed stock has been unissued.

The term Treasury Stock should be restricted to such stock as has already been issued by the company and then returned to the company, frequently by donation. The student should carefully avoid employing the term Treasury Stock for Unsubscribed or Unissued Stock, as practiced by some writers on bookkeeping and accounting.

(Pp. 129–130); H., 146–155; R. C., 128–130; C. O., 89–90.

5. *What are meant by dividends? Who is entitled to dividends? What is the difference between the apportionment of profits among the members of a firm and the voting of dividends by the board of directors of a corporation?*

5. (*a*) Dividends are such portions of the net profit or sur-

plus of a corporation as have been set aside by the directors or "declared" for distribution among the stockholders of record.

(*b*) All stockholders of record are entitled to dividends. A stockholder of record is one whose name is registered in the Stock Ledger as being the owner of stock acquired for value.

(*c*) The profits of a firm are distributed among the members equally, or according to the articles of agreement. The distribution is adjusted by means of a Journal entry and the profits so distributed are frequently left untouched by the members of the concern. The distribution among the members of a corporation is identical in that the profits are distributed in proportion to the interest of each stockholder (represented by holdings of stock). The difference lies in the fact that the "declaration" of dividends leads to the *paying* out of actual money to stockholders, whereas in the partnership, the money is *not* so paid out.

(Pp. 135–138); B. C., 311–318; S. C., 180–191.

6. *Mention three important privileges enjoyed by a corporation which are denied partnerships.*

6. (*a*) Perpetual succession.
   (*b*) To deal in real estate with ease and facility as contrasted with the complexities of partnership holdings.
   (*c*) Limitation of liability of its members.

H. L., 262–263; G. L., 249–252.

7. *Mention two restrictive features applied to corporations which are absent in the case of partnerships.*

7. (*a*) Cannot set up usury as a defense. (In New York.)
   (*b*) *Ultra vires.* It can engage only in such activities as are specified or implied in its charter and by-laws.

H. L., 263, 265–266: G. L., 252, 254; R. C., 14–20; S. L., 217–219; S. C., 53–74.

8. *Outline the steps necessary to incorporate an industrial concern in your state.*

8. In New York State the following steps are necessary:

"A business corporation is formed in New York under the Business Corporations Law (Ch. 4 of the Consolidated Laws of 1909) as follows:

"Prepare three (3) copies of a certificate of incorporation. These certificates should be signed and acknowledged by the incorporators. Send two (2) of them to the Secretary of State, with directions that one (1) be filed and the other be returned as a certified copy of the original. The fees of the Secretary of State are ten dollars ($10.00) for filing the certificate, and fifteen cents (15c.) per folio for recording; for certifying the copy, one dollar ($1.00). At the same time the organization tax should be sent to the State Treasurer. The tax amounts to fifty cents (50c.) per thousand dollars of the total authorized capital stock stated in the certificate; minimum tax, five dollars ($5.00). The State Treasurer will send one receipt to the Secretary of State, who will attach it to the certificate of incorporation and will notify the person from whom he received it that it has been filed. The State Treasurer will also send a duplicate receipt to the remitter, which duplicate receipt should be attached to the third copy of the certificate, which is termed a duplicate original—the other original being filed by the Secretary of State. The duplicate original should then be filed in the office of the County Clerk of the county in which the principal office of the company is to be located. The County Clerk's fees are filing fee, six cents (6c.) per folio; recording fee, ten cents (10c.) per folio."

(From Professor Greendlinger's "Accountancy Problems," ii, 230.)

The certificate of incorporation should contain the clauses as outlined in Elements of Accounting, pages 116-117.

(Pp. 115–118); G. II, 230–231; H. L., 257–258; also consult the corporation laws of your own state.

Group Two

1. *A corporation is organized under the laws of the state of New York, with an authorized capitalization of $1,-000,000.00 divided into shares of the par value of $100.00.*
   - (*a*) *Formulate entries, if all the stock is subscribed for and paid in cash.*
   - (*b*) *If all is subscribed for, and the subscription agreement calls for payment in four equal quarterly installments, and the same are paid accordingly.*
   - (*c*) *If the stock is all subscribed for at $90.00 per share.*
   - (*d*) *Combine* (*c*) *and* (*a*) *above.*
   - (*e*) *It is now found that the company has not sufficient working capital, so the stockholders agree to make a pro rata donation to the treasury of the company of 5 per cent. of their individual holdings.*
   - (*f*) *One-half of the stock contributed is sold at par; the balance at $90.00.*
   - (*g*) *Instead of* (*a*), *if only 80 per cent. had been subscribed for?*

1 (*a*)

a^1	Preamble		
a^2	Subscriptions	$1,000,000.00	
	To Capital Stock		$1,000,000.00
a^3	Cash	1,000,000.00	
	To Subscriptions		1,000,000.00

(*b*)

b^1	Like "a^1"		
b^2	Like "a^2"		
b^3	Installment No. 1	$250,000.00	
	Installment No. 2	250,000.00	
	Installment No. 3	250,000.00	
	Installment No. 4	250,000.00	
	To Subscriptions		$1,000,000.00
b^4	Cash	250,000.00	
	To Installment No. 1		250,000.00

(Similarly for the other installments, as paid.)

(*c*)

c^1	Like "a^1"		
c^2	Subscriptions	$900,000.00	
	*Discount on Stock	100,000.00	
	To Capital Stock		$1,000,000.00
c^3	Cash	900,000.00	
	To Subscriptions		900,000.00

(*In New York State it is illegal to issue stock below par. This entry is made on the assumption that the transaction was for a corporation organized under the laws of a state permitting the issuing of stock below par.)

(*d*) The combination of problem "c" and "a" has been shown in "c." The specific answer to "c" above was the entry for the subscription "c^2." The specific answer to the combination of "c" and "a," was shown under the headings "c^1," "c^2," "c^3."

(*e*)

	Treasury Stock	$50,000.00	
	To Working Capital Suspense		$50,000.00

(*f*)

f^1	Cash	47,500.00	
	Working Capital Suspense	2,500.00	
	To Treasury Stock		50,000.00
f^2	Working Capital Suspense	47,500.00	
	To Working Capital		47,500.00

(*g*)

g^1	Same as a^1		
g^2	Subscriptions	$800,000.00	
	Unsubscribed Stock	200,000.00	
	To Capital Stock		$1,000,000.00
g^3	Cash	800,000.00	
	To Subscriptions		800,000.00

(Pp. 121–133); B. C., 216–227.

2. *What would be the entry if the corporation referred to in Exercise 1 issued first mortgage bonds, a first lien on all their property, to the amount of $50,000.00 and floated them at par?*

2

(*a*) Cash $50,000.00
To First Mortgage Bonds Payable $50,000.00

(*b*) The foregoing entry is reduced to its simplest terms. In actual practice, the following is really in accordance with the facts:

(1) Unsubscribed Bonds Payable $50,000.00
To Bond Authorization $50,000.00

(2) Subscriptions to Bonds 50,000.00
To Unsubscribed Bonds Payable 50,000.00

(3) Cash 50,000.00
To Subscriptions to Bonds 50,000.00

(4) Bond Authorization 50,000.00
To First Mortgage Bonds Payable 50,000.00

(Pp. 133–135.)

3. *Assuming that the underwriting expenses had amounted to $5,000.00, what would be the entry?*

3

Underwriting Expenses (or Organization Expenses) $5,000.00
To Cash $5,000.00

(P. 134.)

4. *If the capital stock were to be increased to $2,000.00, what entry, if any, would be made at the time of authorization? At the time of subscription?*

4

(*a*) Unsubscribed Stock $1,000,000.00
To Capital Stock $1,000,000.00

(*b*) Subscriptions 1,000,000.00
To Unsubscribed Stock 1,000,000.00

5. *If, in (a) of Exercise 1, the authorized capitalization had been for 25 per cent. preferred stock and 75 per cent. common stock, what would be the entry?*

5

(a) Preamble

(b)	Subscriptions to Common Capital Stock	$750,000.00	
	Subscriptions to Preferred Capital Stock	250,000.00	
	To Common Capital Stock		$750,000.00
	Preferred Capital Stock		250,000.00
(c)	Cash	$1,000,000.00	
	To Subscriptions to Common Capital Stock		$750,000.00
	Subscriptions to Preferred Capital Stock		250,000.00

(P. 131.)

6. *The New Manufacturing Co. is organized under the laws of the State of New York, with an authorized capital of $1,000,000.00 divided into shares of $100.00 each. The board of directors has regularly decided to issue $450,000.00 of stock for the business of A. and F., and $500,000.00 for that of the Old Manufacturing Co., a corporation organized under New York laws. Following is the accepted Balance Sheet of A. & F. at the date of purchase:*

Assets: cash, $5,000.00; notes receivable, $210,000.00; accounts receivable, $140,000.00; plant and machinery, $200,000.00; A.'s Drawing Account, $1,000.00; liabilities: notes payable, $100,000.00; accounts payable, $56,000.00; A.'s Capital Account, $250,000.00; F.'s Capital Account, $150,000.00.

The accepted Balance Sheet of the Old Manufacturing Co. is as follows:

Assets: cash, $50,000.00; notes receivable, $100,000.00; accounts receivable, $200,000.00; plant and machinery, $150,000.00; good will, $100,000.00; liabilities: notes payable, $50,000.00; mortgage payable, $100,000.00; capital stock, $450,000.00.

(a) Make closing entries in books of A. & F.

(*b*) *Make opening entries in books of New Manufacturing Co.*

(*c*) *Prepare Balance Sheet of New Manufacturing Co.*

6 (*a*) The closing entries in the books of A. & F.:

(1) The entire business of A. and F., a copartnership, has this day been sold to the New Manufacturing Company, a corporation, organized under the laws of the State of New York, for $450,000.00 of the stock of the said corporation. The following entries are made for the purpose of closing our books:

(2)	A, Capital	$1,000.00	
	To A, Drawing		$1,000.00
	To transfer Mr. A's drawing account to his capital account.		
(3)	Goodwill	$51,000.00	
	To A, Capital		$25,500.00
	F, Capital		25,500.00
	The New Manufacturing Company's purchase price was $450,000.00 which is $51,000.00 in excess of the book valuation of our net capital. This excess, *goodwill*, is equally distributed between Messrs. A & F, as a profit on the transaction.		
(4)	The New Manufacturing Co.	$606,000.00	
	To Cash		$5,000.00
	Notes Receivable		210,000.00
	Accounts Receivable		140,000.00
	Plant and Machinery		200,000.00
	Goodwill		51,000.00
	For the purpose of transferring all the assets of this company, including goodwill, to the New Manufacturing Company.		
(5)	Notes Payable	$100,000.00	
	Accounts Payable	56,000.00	
	To New Manufacturing Co.		$156,000.00
	The New Manufacturing Co. assumed all the existing liabilities of this firm.		
(6)	New Manufacturing Co. Stock	$450,000.00	
	To New Manufacturing Co.		$450,000.00

Received 4500 shares of the stock of the New Manufacturing Co., in full payment of all claims against them.

(7)	A, Capital	$274,500.00	
	F, Capital	175,500.00	
	To New Manufacturing Co. Stock		$450,000.00

Distribution of stock in full settlement of all claims of Mr. A and of Mr. F, as follows:
Mr. A 2,745 shares
Mr. F 1,755 shares

(*b*) Opening entries on the books of the New Manufacturing Co.:

(1) THE NEW MANUFACTURING COMPANY
incorporated under the laws of the
State of New York on........, 19....
with an authorized capital of
$1,000,000.00
divided into 10,000 shares, each of a
par value of $100.00

(2)	Subscriptions	$950,000.00	
	Unsubscribed Stock	50,000.00	
	To Capital Stock		$1,000,000.00

Subscribers:
A & F $450,000.00
Old Mfg. Co. 500,000.00

(3)	Sundry Assets of A & F	$606,000.00	
	To Sundry Liabilities of A & F		$156,000.00
	Subscriptions		450,000.00

Business of Messrs. A & F acquired as per agreement dated .... See Minute Book, page.......

(4)	Sundry Assets of Old Mfg. Co.	$650,000.00	
	To Sundry Liabilities of Old Mfg. Co.		$150,000.00
	Subscriptions		500,000.00

Business of Old Manufacturing Co. acquired as per agreement dated .... See Minute Book, page .....

(5)	Cash	$5,000.00	
	Notes Receivable	210,000.00	
	Accounts Receivable	140,000.00	
	Plant and Machinery	200,000.00	
	Goodwill	51,000.00	
	To Sundry Assets of A & F		$606,000.00

For the purpose of closing the credit account (above) and placing upon the books the assets acquired.

(6)	Sundry Liabilities of A & F	$156,000.00	
	To Notes Payable		$100,000.00
	Accounts Payable		56,000.00

For the purpose of closing the Sundry Liabilities of A & F Account, and placing their liabilities, assumed by us, on the books.

(7)	Cash	$50,000.00	
	Notes Receivable	100,000.00	
	Accounts Receivable	200,000.00	
	Plant and Machinery	150,000.00	
	Goodwill	150,000.00	
	To Sundry Assets of Old Mfg. Co.		$650,000.00

For the purpose of closing the credit account (above) and placing upon the books the assets acquired.

(8)	Sundry Liabilities of Old Mfg. Co.	$150,000.00	
	To Notes Payable		$50,000.00
	Mortgage Payable		100,000.00

For the purpose of closing the Sundry Liabilities of Old Mfg. Co. Account, and placing their liabilities, assumed by us, on the books.

(*c*)

Balance Sheet of New Manufacturing Company

(DATE)

ASSETS		LIABILITIES AND CAPITAL		
Cash	$55,000.00	Notes Payable		$150,000.00
Notes Receivable	310,000.00	Accounts Payable		56,000.00
Accounts Receivable	340,000.00	Mortgage Payable		100,000.00
Plant and Machinery	350,000.00			
Goodwill	201,000.00	Total Liabilities		$306,000.00
		CAPITAL		
		Auth. Capital Stock	$1,000,000.00	
		Less Unsub. Stock	50,000.00	
		Outstdg. Capital Stock		$950,000.00
	$1,256,000.00			$1,256,000.00

(Pp. 145–154); G. II, 23–27, 78–83, 175–176, 183–184; R. C., 315–337.

7. *A corporation has an authorized capital of $100,000.00, of which 80% has been issued. The Profit and Loss Account shows a net profit of $18,000.00. The Board of Directors declares a dividend of 10%.*
   - (*a*) *Show entries for the declaration of dividends and to close the Profit and Loss Account.*
   - (*b*) *Show entry when L. M. Rich, the owner of sixteen shares of stock, is paid his dividend by check.*

7.

		Dr.	Cr.
(*a*)	Profit and Loss	$18,000.00	
	To Dividends Payable		* $8,000.00
	Surplus		10,000.00

(*Dividends are declared on capital stock, not on profits.)

		Dr.	Cr.
(*b*)	Dividends Payable	$160.00	
	To Cash		$160.00

(Pp. 136–138); B. C., 227–229; R. C., 190–191.

8. *Suppose that the partnership of F. & G. (Exercise 8, page 37) were changed to a corporation under the laws of the State of New York, on February 1, 1914, with an authorized capital of $50,000.00, divided into shares of $100.00 each.*

   (*a*) *If all of the stock had been distributed to Messrs. F. and G., show the entries to close the partnership books and to open the corporation books.*

   (*b*) *If only $40,000.00 of stock had been given to Messrs. F. and G., show the corresponding entries in the old and in the new books.*

   (*c*) *If only $30,000.00 of stock had been so given to Messrs. F. and G., required, the corresponding entries.*

8 (*a*) To close the old books:

(1) February 1, 1914

THE F & G COMPANY
has this day incorporated
under the laws of the State of New York
with an authorized capital of
$50,000.00
divided into shares of $100.00 each

The following entries are made to close the old books, and to transfer all our assets and liabilities to the F & G Co., a corporation.

(2) Goodwill	$18,000.00	
To F, Capital		$9,000.00
G, Capital		9,000.00

Excess valuation placed upon this business by the F & G Co., a corporation, to which Messrs. F & G have agreed to sell their business as per articles of agreement executed this day.

(3)	F & G Co.	$76,500.00	
	To Cash		$12,000.00
	Notes Receivable		10,000.00
	Accounts Receivable		24,000.00
	Merchandise		10,000.00
	Fixtures		2,500.00
	Goodwill		18,000.00

To transfer all our assets to the F & G Co., a corporation, as per agreement.

(4)	Notes Payable	$15,500.00	
	Accounts Payable	11,000.00	
	To F & G Co.		$26,500.00

Assumption by the F & G Co., a corporation, of the existing liabilities of this firm, as per agreement.

(5)	F & G Co. Stock	$50,000.00	
	To F & G Co.		$50,000.00

Received in full payment as per contract, 500 shares of stock, par value, $100.00.

(6)	F, Capital	$26,000.00	
	G, Capital	24,000.00	
	To F & G Co. Stock		$50,000.00

Distribution of 500 shares of F & G Co.'s stock in full payment of all the rights and interests in the firm of F & G, as follows:

Mr. F 260 shares
Mr. G 240 shares

To open the new books:

(1) February 1, 1914

THE F & G COMPANY
have this day incorporated under
the laws of New York State with an
authorized capital of
$50,000.00
divided into shares of $100.00 each

(2)	Subscriptions	$50,000.00	
	To Capital Stock		$50,000.00

Subscription to all of the stock of this company as follows:
F 260 shares
G 240 shares

(3)	Cash	$12,000.00	
	Notes Receivable	10,000.00	
	Accounts Receivable	24,000.00	
	Merchandise	10,000.00	
	Fixtures	2,500.00	
	Goodwill	18,000.00	
	To Notes Payable		$15,500.00
	Accounts Payable		11,000.00
	Subscriptions		50,000.00

Payment for subscriptions to 500 shares of stock in this Company, as per Minute Book, and as per agreement.

(*b*) To close the old books:

February 1, 1914

(1) F & G have this day incorporated under the laws of New York State. The following entries are made to close the old books and transfer all our assets and liabilities to the F & G Co., a corporation.

(2)	Goodwill	$8,000.00	
	To F Capital		$4,000.00
	G Capital		4,000.00

Excess valuation placed upon this business by the F & G Co., a corporation, to which Messrs. F & G agreed to sell their business as per articles of agreement.

(3)	F & G Co.	$66,500.00	
	To Cash		$12,000.00
	Notes Receivable		10,000.00
	Accounts Receivable		24,000.00
	Merchandise		10,000.00
	Fixtures		2,500.00
	Goodwill		8,000.00

To transfer all our assets to the F & G Co., a corporation, as per articles of agreement.

(4)	Notes Payable	$15,500.00	
	Accounts Payable	11,000.00	
	To F & G Co.		$26,500.00

Assumption by the F & G Co., a corporation, of the existing liabilities of this firm as per articles of agreement.

(5)	F & G Co. Stock	$40,000.00	
	To F & G Co.		$40,000.00

Received in full payment, as per articles of agreement, 400 shares of stock, par value, $100.00.

(6)	F Capital	$21,000.00	
	G Capital	19,000.00	
	To F & G Co.'s Stock		$40,000.00

Distribution of 400 shares of F & G Co. stock in full payment of all the rights and interests in the firm of F & G, as follows:

Mr. F	210 shares
Mr. G	190 shares

To open the new books:

February 1, 1914

(1)

THE F & G COMPANY
have this day incorporated
under the laws of New York State
with an authorized capital of
$50,000.00
divided into shares of $100.00 each

(2)	Subscriptions	$40,000.00	
	Unsubscribed Stock	10,000.00	
	To Capital Stock		$50,000.00

Subscriptions to 400 shares of stock, as follows:
F 210 shares
G 190 shares

(3)	Cash	$12,000.00	
	Notes Receivable	10,000.00	
	Accounts Receivable	24,000.00	
	Merchandise	10,000.00	
	Fixtures	2,500.00	
	Goodwill	8,000.00	
	To Notes Payable		$15,500.00
	Accounts Payable		11,000.00
	Subscriptions		40,000.00

Accepted in full payment of F & G's subscriptions to 400 shares of stock in this Company, as per contract and as per Minute Book.

(*c*) To close the old books:

(1) F & G have this day incorporated under the laws of New York State. The fol-ing entries are made to close the old books and transfer all our assets and liabilities to the F & G Co., a corporation.

(2)	F & G Co.	$58,500.00	
	To Cash		$12,000.00
	Notes Receivable		10,000.00
	Accounts Receivable		24,000.00
	Merchandise		10,000.00
	Fixtures		2,500.00

To transfer all our assets to the F & G Co., a corporation, as per contract.

(3)	Notes Payable	$15,500.00	
	Accounts Payable	11,000.00	
	To F & G Co.		$26,500.00

Assumption by the F & G Co., a corporation, of the existing liabilities of this firm as per contract.

(4)	F & G Co.* Stock	$30,000.00	
	*Profit and Loss	2,000.00	
	To F & G Co.		$32,000.00

Received in full payment as per agreement, 300 shares of stock, par value, $100.00.

(5)	F, Capital	$1,000.00	
	G, Capital	1,000.00	
	To Profit and Loss		$2,000.00

To divide the loss incurred on the sale of our business to the F & G Co., and to close the Profit and Loss Account.

(6)	F, Capital	$16,000.00	
	G, Capital	14,000.00	
	To F & G Co. Stock		$30,000.00

Distribution of 300 shares of F & G Co.'s stock in full payment of all the rights and interests in the firm of F & G, as follows:

Mr. F 160 shares
Mr. G 140 shares

(*By charging the capital accounts of Messrs. F & G immediately, entry "5" would be avoided.)

To open the new books:

(1)

February 1, 1914

THE F & G COMPANY
have this day incorporated
under the laws of New York State
with an authorized capital of
$50,000.00
divided into shares of $100.00 each

(2)	Subscriptions	$30,000.00	
	Unsubscribed Stock	20,000.00	
	To Capital Stock		$50,000.00

Subscriptions to 300 shares of stock as follows:
F 160 shares
G 140 shares

(3)	Cash	$12,000.00	
	Notes Receivable	10,000.00	
	Accounts Receivable	24,000.00	
	Merchandise	10,000.00	
	Fixtures	2,500.00	
	To Notes Payable		$15,500.00
	Accounts Payable		11,000.00
	*Reserve		2,000.00
	Subscriptions		30,000.00

Accepted in full payment of F & G's subscriptions to 300 shares of stock in this Company, as per contract.

(Pp. 138–145); B. C., 233–236; R. C., 299–315.

9. *L. E. Smythe (Exercise 1, page 24) incorporates a company with a Capital Stock of $10,000.00, of which he takes $8,000.00 in full payment of his business. He secures outside subscriptions to $1,500.00 of the remaining stock, and this amount is paid in cash.*

(*a*) *Required, the entries to close the old books.*

(*b*) *Required, the entries to open the new books.*

(*Introduce modern labor-saving devices.*)

*(Or Surplus.)

9 (*a*) Entries to close the old books (after Exercise 3, Group Two, page 26):

March 31, 1913

(1) L. E. Smythe has this day incorporated under the laws of New York State. The following entries are made to close the old books and to transfer all assets and liabilities to the L. E. Smythe Co.

(2) Goodwill	$2,660.00	
To L. E. Smythe, Capital		$2,660.00

Excess valuation placed upon the business of L. E. Smythe, by the L. E. Smythe Co., a corporation, to which Mr. Smythe has agreed to sell his business as per contract.

(3) L. E. Smythe Co.	$17,990.00	
To Cash		$6,580.00
Merchandise		3,400.00
Fixtures		300.00
Notes Receivable		200.00
Accounts Receivable		4,850.00
Goodwill		2,660.00

To transfer all our assets to the L. E. Smythe Co., as per agreement.

(4) Notes Payable	$8,000.00	
Accounts Payable	1,990.00	
To To L. E. Smythe Co.		$9,990.00

Assumption by the L. E. Smythe Co. of the existing liabilities of this business, as per agreement.

(5) L. E. Smythe Co. Stock	$8,000.00	
To L. E. Smythe Co.		$8,000.00

Received in full payment 80 shares of stock as per agreement, at $100 per share.

(6) L. E. Smythe, Capital	$8,000.00	
To L. E. Smythe Co. Stock		$8,000.00

Distribution of 80 shares of L. E. Smythe & Co.'s stock in full payment as per contract.

(*b*) To open the new books:

Accts. Pay.	General	L.F.		L.F.	General	Accts. Rec.
			March 31, 1913			
			THE L. E. SMYTHE COMPANY has this day incorporated under the laws of New York State with an authorised capital of $10,000.00 divided into 100 shares of $100.00 each			
			31			
	9,500 00		Subscriptions			
	500 00		Unsubscribed Stock			
			To Capital Stock		10,000 00	
			Subscriptions as follows:			
			L. E. Smythe, 80 shares			
			"Miscellaneous" 15 shares			
			31			
	6,580 00		Cash			
	3,400 00		Merchandise			
	300 00		Fixtures			
	200 00		Notes Receivable			
	4,850 00		Accounts Receivable:			
			Bailey & Co. $495.			
			R. Sommers 1,365.			
			Jansen & Rowe 2,400.			
			T. L. Sellers 590.			
	2,660 00		Goodwill			
			To Notes Payable		8,000 00	
			Accounts Payable:		1,990 00	
			Cole & Johnson $1,500.			
			Allis & Co. 490.			
			Subscriptions		8,000 00	
			Accepted L. E. Smythe's business in full payments of his subscriptions to 80 shares of stock in this Company, as per articles of agreement executed this day.			
			31			
	1,500 00		Cash			
			To Subscriptions		1,500 00	
			Received cash in full, from miscellaneous subscribers.			

(Pp. 138–145.)

SOLUTIONS TO EXERCISES

CHAPTER VII

BALANCE SHEETS AND TRADING AND PROFIT AND LOSS ACCOUNTS

Group One

1. *Differentiate between (a) Trial Balance; (b) Statement of Assets and Liabilities; (c) Balance Sheet.*

1. (*a*) A Trial Balance is a summary of the balances of all the accounts. All of these accounts appear in the Ledger, though sometimes some of the accounts appear elsewhere, as for example, the Cash Account, in the Cash Book. There are two kinds of Trial Balances—Trial Balance of Totals and Trial Balance of Differences. The latter is the more practical one, and it is the one we have in mind when we discuss *the* Trial Balance.

(*b*) A Statement of Assets and Liabilities is a summarized exhibit of all the assets of the business arranged so as to correspond to the liabilities similarly arranged; the difference between the two sides, if the assets are greater, is the *Net Capital,* but if the liabilities are greater the difference is called *Deficit.*

(*c*) A Balance Sheet is for all practical purposes the same as the Statement of Assets and Liabilities. The technical distinction is that the Balance Sheet is taken from books kept by double entry *after* they have been closed, *i. e.,* after the transfer of the nominal accounts and the setting up of inventories.

(Pp. 160-162.)

2. *State the essential differences between a Trading and Profit and Loss Statement and a Trading and Profit and Loss Account.*

2. The essential difference between the Trading and Profit and Loss Statement and the Trading and Profit and Loss Account is that the latter is in the Ledger while the former is arranged in a more or less non-technical form for presentation to people usually not bookkeeping experts.

(Pp. 175–176.)

3. *What are deferred assets? Give three examples.*

3. Deferred assets are assets which ordinarily are charged to nominal (Profit and Loss) accounts, but which have not yet been destroyed or used up. Examples of deferred assets are Unconsumed Advertising Prepaid, Accrued Interest Receivable, Unconsumed Fuel, etc. (Deferred assets are sometimes called Deferred Charges to Income, Deferred Charges, Debit Expense Inventories, and Accruals.)

(See references for Exercise 4, below.)

4. *What are deferred liabilities? Give three examples.*

4. Deferred Liabilities are liabilities which are not yet due or payable. Examples: Interest Payable but not yet due (accrued interest on notes, bonds and mortgages, etc.), Salary Accrued (not yet due or payable because at the time the books were closed the payroll period had not been completed), similar Wages Accrued, Taxes Accrued, etc. (Deferred Liabilities are also called Deferred Credit Items; Liability Inventories, Accruals).

(P. 165); M., 97–99, 116, 272, 400; H., 118–120, 123.

5. *State clearly the reasons for sectionalizing the Balance Sheet.*

5. Sectionalizing the Balance Sheet has probably been carried to an extreme. The practical purpose for segregating items is to bring together current assets, so as to compare them with current liabilities. This practice is especially followed by credit men for the purpose of ascertaining the "healthfulness" of a

business. On the basis of this need, accountants have frequently advocated the practice of sectionalizing or separating both asset and liability items into other groups; frequently it is a benefit to ascertain clearly the value of working or trade assets; fixed assets; fixed liabilities, etc., but for most practical purposes the division into current and other assets, current and other liabilities, is quite sufficient.

(Pp. 162–166); M., 213–223; H., 41–55; E., 407–410.

6. *Name the sections of a modern Balance Sheet and give the titles of two accounts in each section.*

6. On the left side:

(*a*) Current Assets (Examples: Cash, Accounts Receivable).

(*b*) Deferred Assets (Examples: Prepaid Advertising, Unconsumed Fuel).

(*c*) Working or Trade Assets (Examples: Goods in Process, Raw Materials).

(*d*) Fixed Assets (Examples: Plant and Machinery, Tools).

On the right side:

(*a*) Current Liabilities (Examples: Accounts Payable, Notes Payable).

(*b*) Deferred Liabilities (Examples: Interest Payable Accrued, Wages Accrued).

(*c*) Fixed Liabilities (Mortgage Payable, Bonds Payable).

(*d*) Capital and Surplus (Applicable to a corporation).

(Examples:

1. Common Capital Stock, Preferred Capital Stock.
2. Reserves, Surplus.)

7. *What is meant by closing the Ledger? How does this process affect the accounts of the Ledger?*

7. "Closing the Ledger" means to enter into the Ledger, under proper titles, all asset and liability inventories, and to transfer all profit and loss (nominal) items to a summary Profit and Loss Account and the distribution of the result of the Profit and Loss Account to certain other accounts. (In partnerships to the partners' accounts; in corporations to surplus, dividends, reserves, etc.) The effect of closing the Ledger is to remove every nominal account from the Ledger, so that those which still remain are assets, liabilities or capital items. It is these accounts which remain after the Ledger is closed, and that enter into the construction of the Balance Sheet.

(Pp. 16–17, 175–176); H., 40–41.

8. *How is "Accrued Interest on Mortgage" Account affected by the subsequent payment of the interest?*

8. When the interest on mortgage is paid the payment represents a cancellation of "Accrued Interest on Mortgage," which was entered as a liability at the end of the previous period, and the interest which is applicable to the current period. Accordingly, the payment cancels the item formerly carried to "Accrued Interest on Mortgage" account, and opens a Profit and Loss or Nominal account with "Interest on Mortgage" account for the difference between the amount of the payment and the amount formerly carried to Accrued Interest Account.

9. *How do you treat the following items in the Balance Sheet, in the Trading and Profit and Loss Statement, or in both?*
(a) Notes Receivable Discounted Account; (b) unsubscribed stock; (c) unpaid wages; (d) taxes accrued but not due; (e) coal, charged to Fuel Account, unconsumed.

9. (*a*) Notes Receivable Discounted Account is shown as a deduction from the Notes Receivable Account among the current assets in the Balance Sheet; it does not appear in the Profit and Loss Statement.

(*b*) Unsubscribed stock appears as a deduction from Capital Stock shown on the liability side of the Balance Sheet in the section headed "Capital and Surplus"; it does not affect the Profit and Loss Statement.

(*c*) Unpaid Wages is shown as a deferred liability among the deferred liability items in the Balance Sheet; it is added to the amount appearing in the Wages Account as shown in the Ledger, and is carried to the prime cost division of the Manufacturing section of the Profit and Loss Statement.

(*d*) Taxes Accrued Account appears under the same heading as Unpaid Wages on the Balance Sheet; it is shown as an addition to taxes, if the Tax Account existed, in that section of the Profit and Loss Statement to which the taxes were chargeable.

(*e*) Unconsumed Fuel is shown as a deferred asset among the deferred asset items on the Balance Sheet; it also appears as a deduction from the Fuel Account in the Overhead division of the Manufacturing Section of the Profit and Loss Statement.

Group Two

1. *William A. Topper and George F. Hinds commenced a partnership on April 1, 1912. On March 30, 1913, they found that the value of their unsold merchandise, at cost, was $6,280.00. Their office furniture was estimated to be worth $800.00. They had paid their rent until May 1, 1913, at $100 per month. They owed about $150 to their lawyer, who had rendered no bill, while their payroll, not due till April 2, already amounted to $310.00. The Trial Balance shown on the next page was taken from their books.*

You are requested to:

(*a*) *Prepare a modern Balance Sheet.*

(*b*) *Prepare a modern Trading and Profit and Loss Statement.*

(*c*) *Frame Journal entries to close the Ledger.*

(*d*) *Prepare a Trading and Profit and Loss Account.*

Trial Balance

Cash	$4,312.00	
Petty Cash	64.50	
Mdse. Inventory, 4/1/12	2,500.00	
William A. Topper, Drawing a/c	200.00	
Purchases	18,000.00	
Sales		$31,181.50
Sales Returns	400.00	
Returned Purchases		325.00
Accounts Receivable	7,000.00	
Notes Payable		2,500.00
Notes Receivable	5,000.00	
Accounts Payable		3,800.00
Rent	1,200.00	
Office Furniture	1,350.00	
Discount on Purchases		180.00
Selling Expenses	2,000.00	
Expense	3,600.00	
Salesmen's Salaries	2,000.00	
Salaries	1,300.00	
Notes Receivable Discounted		1,000.00
Discount on Notes	60.00	
William A. Topper, Capital		5,000.00
George F. Hinds, Capital		5,000.00
	$48,986.50	$48,986.50

1 (*a*)

Balance Sheet of Topper & Hinds

AS OF MARCH 31, 1913

ASSETS			LIABILITIES AND CAPITAL		
Current Assets:			Current Liabilities:		
Cash		$4,312.00	Accts. Pay.	$3,800.00	
Petty Cash		64.50	Notes Pay.	2,500.00	$6,300.00
Accts. Rec.		7,000.00			
Notes Rec.	$5,000.00		Other Liabilities:		
Less Dis. Notes	1,000.00	4,000.00	Accrued Exp.	$150.00	
			Accrued Sal.	310.00	460.00
		$15,376.50			
Other Assets:					
Prepaid Rent		$100.00	Capital:		
Merchandise Inventory		6,280.00	Wm. A. Topper	$7,798.25	
Office Furniture		800.00	Geo. F. Hinds	7,998.25	
					$15,796.50
		$22,556.50			$22,556.50

(b)

Trading and Profit and Loss Statement of Topper & Hinds

FOR THE YEAR ENDED MARCH 31, 1913

TRADING SECTION

Mdse. Inv. April 1/12		$2,500.00	Sales	$31,181.50	
Purchases	$18,000.00		Less Returns	400.00	
Less Returns	325.00	17,675.00			
			NET SALES		$30,781.50
		$20,175.00			
Less Inv., Mch. 30, 1913		6,280.00			
(TURNOVER)		$13,895.00			
Selling Expenses		2,000.00			
Salesmen's Salaries		2,000.00			
Gross Profit on Trading Carried to Administration Section		12,886.50			
		$30,781.50			$30,781.50

ADMINISTRATION SECTION

Expenses	$3,600.00		Gross Profit on Trading, brought down	$12,886.50
Accrued	150.00	$3,750.00		
Salaries	$1,300.00			
Accrued	310.00	1,610.00		
Rent	$1,200.00			
Less prepaid	100.00	1,100.00		
Depreciation on office furniture		550.00		
Gross Business Profit carried to Profit and Loss Section		5,876.50		
		$12,886.50		$12,886.50

PROFIT AND LOSS SECTION

Discount on Notes	$60.00	Gross Business Profit, brought down	$5,876.50
Net Business Profit	5,996.50	Discount on Purchases	180.00
	$6,056.50		$6,056.50

(c) MARCH 31, 1913

Returned Purchases	$325.00	
To Purchases		$325.00
31		
Purchases	2,500.00	
To Mdse. Inventory		2,500.00
31		
Mdse. Inventory	6,280.00	
To Purchases		6,280.00
31		
Trading Account	13,895.00	
To Purchases		13,895.00
31		
Trading Account	4,000.00	
To Selling Expenses		2,000.00
Salesmen's Salaries		2,000.00
31		
Sales	400.00	
To Sales Returns		400.00
31		
Sales	30,781.50	
To Trading Account		30,781.50
31		
Trading Account	12,886.50	
To Administration Account		12,886.50
31		
Expenses	150.00	
To Expenses Accrued		150.00
31		
Salaries	310.00	
To Salaries Accrued		310.00
31		
Prepaid Rent	100.00	
To Rent		100.00
31		
Administration Account	7,010.00	
To Expenses		3,750.00
Salaries		1,610.00
Rent		1,100.00
Office Furniture		550.00

31			
Administration Account		$5,876.50	
To Profit and Loss Account			$5,876.50
31			
Discount on Purchases		180.00	
To Profit and Loss Account			180.00
31			
Profit and Loss Account		60.00	
To Discount on Notes			60.00
31			
Profit and Loss Account		5,996.50	
To William A. Topper, Capital*			2,998.25
George F. Hinds, Capital			2,998.25

(*d*)

TRADING ACCOUNT

1913				1913			
March 31	Purchases	J..	$13,895.00	March 31	Sales	J..	$30,781.50
	Sundries		4,000.00				
	Administration Acct.		12,886.50				
			$30,781.50				$30,781.50

ADMINISTRATION ACCOUNT

1913				1913			
March 31	Sundries	J..	$7,010.00	March 31	Trading Account	J..	$12,886.50
	Profit and Loss Acct.		5,876.50				
			$12,886.50				$12,886.50

PROFIT AND LOSS ACCOUNT

1913				1913			
March 31	Dis. on Notes	J..	$60.00	March 31	Administration Acct.	J..	$5,876.50
	Wm. A. Topper, Cap.		2,998.25		Dis. on Purchases		180.00
	Geo. F. Hinds, Cap.		2,998.25				
			$6,056.50				$6,056.50

(Chaps VII and IX.)

*(or Drawing Account.)

All Gilman
P 3-8
Res + Res. funds

SOLUTIONS TO EXERCISES

CHAPTER VIII

DEPRECIATION, RESERVE, SINKING FUND AND INVESTMENT ACCOUNTING

Group One

1. *Distinguish between a Reserve Fund Account and a Reserve Account.*

1. The Reserve Fund Account always has a debit balance; the Reserve Account has a credit balance. The Reserve Fund Account is an asset; the Reserve Account represents retained profits. The Reserve Fund Account is created by crediting cash and debiting the fund account; the Reserve Account is created by charging surplus and crediting Reserve Account. The object of the Reserve Account is to retain profits so that they will not be declared as dividends; the object of the Reserve *Fund* Account is to set aside some cash so as to have money available positively, in case of need or whenever the object for which the fund has been created, or the reserve set aside, is reached. The Reserve Fund Account may be established at the beginning of a business before operations have commenced or profits have been earned; the Reserve Account, in general, can only be established when profits have been earned; after the reserve has been established it may be desirable to set aside some cash, either to parallel the Reserve Account or to assure it, so to speak. In the latter case, the amount of the fund must not exactly correspond to the amount of the Reserve Account.

(Pp. 189–195, 197–198); H., 248–250; D. D., 47–56; R. C., 154–155; W. A., 147–148; J., Vol. 6, 394–399, Vol. 7, 185–191, Vol. 9, 352–357, Vol. 10, 267–274, Vol. 11, 261–266, Vol. 16, 358–365; E., 293.

2. *Show in what respect surplus and reserves are identical, and also how they differ.*

2. Reserves and surplus are identical in that both represent retained profits. Surplus is available for dividends while reserves are usually created (by charging surplus) so as to remove some profits from immediate dividend possibility. In this sense, then, it may be said that reserves are profits one step further removed from dividends than surplus. But it must never be forgotten that in times of need, *i. e.,* when the business has suffered a loss or when it is called upon to meet unexpected losses due to an emergency, neither surplus nor reserves are in reality immune from depletion.

(Pp. 196–197); W. A., 174–175; E., 369.

3. *Describe what is meant by depreciation and show what evil results might follow by not taking it into consideration.*

3. Depreciation, in general, refers to the decreased value of property consequent upon wear and tear. It also refers to this decreased value due to age and also to decreased comparative efficiency, due to the fact that new inventions constantly appear upon the market and make it unprofitable to continue in use machinery and tools which are almost as good as when first acquired. The evil which results from not taking depreciation into consideration, *i. e.,* from not charging to some nominal account the decreased value due to wear and tear, age, and obsolescence, is that the cost of manufacturing or the cost of production would appear upon the books at *less* than real cost. For it cannot be denied that the decreased value due to the use of a machine is really a charge against the cost of production.

2 (P. 184–189); H., 121, 134; M., 317–320; D. D., 1–4; R. C., 156–158; W. A., 34–240; J., Vol. 13, 241–243.

4. *Distinguish briefly between Depreciation Account and Reserve for Depreciation Account.*

4. Depreciation Account and Reserve for Depreciation Account are frequently synonymous terms. When synonymous nothing need be said about them, save the criticism that it is unfortunate to employ two terms for the same thought. But there should be a real difference between them. The Depreciation Account should be a "valuation" account, which Professor Hatfield so ably describes in his "Modern Accounting." It should be the account which is taken as an off-set against the corresponding asset in order to determine the book value of that asset. The Reserve for Depreciation account *should* represent a retention of profits, by charging surplus for the purpose of *anticipating* future depreciation. Thus, whereas depreciation is a fact, reserve for depreciation is a prophecy; whereas depreciation is a charge against some nominal account, reserve for depreciation is a charge against Surplus for the purpose of retaining profits; whereas depreciation enters into the cost of production, reserve for depreciation does *not* affect the cost of production.

(Pp. 195–196); D. D., 47–49; J., Vol. 9, 29–35.

Group Two

1. *As the accountant for a factory, how would you decide upon the proper annual allowance on a machine costing $15,000.00 which had just been installed?*

1. The amount to be charged for annual depreciation would depend upon the following factors:
   (1) The probable life of the machine.
   (2) The residual value.

By probable life we mean not only the probable length of physical existence, but the probable length of efficient existence, *i. e.,* how long before the machine would have to be discarded due to the fact that later inventions would make the continued use of the machine unprofitable. Assuming that by consultation with the factory officials and with com-

petent engineers, it was decided that the machine had a probable life of six years, while its residual value would be \$1,000.00, the problem would resolve itself to a determination of the depreciation which should be charged so as to pro-rate equitably this depreciation of \$14,000.00 during a period of six years. The method which I would pursue would not be the simplest one, *i. e.,* dividing \$14,000.00 by six and deciding upon an annual charge for depreciation amounting to \$2,333.33, but I would apply the formula described on pages 187-189 of Elements of Accounting, and known as the Method of Fixed Percentage on Declining Value. I would substitute in the following formula:

$$r = 1 - n\sqrt{\frac{V_2}{V_1}}$$

the given values, thus:

$$r = 1 - \sqrt{\frac{1{,}000}{15{,}000}}$$

The resulting per cent. would be the rate of annual depreciation. I would then construct a table of depreciation, such as shown on page 188 of Elements of Accounting, so that the bookkeeper could write off the amount of annual depreciation without difficulty.

(Pp. 186–189); H., 127–133; M., 320–327; D. D., 28–36; J., Vol. 5, 189–200, Vol. 9, 104–113, Vol. 13, 243–250, Vol. 17, 325–354; E., 296–298.

the amount that will am[illegible] to \$1,000 in 15

2. (*a*) *How much should be set aside each year so that at the maturity of a fifteen-year mortgage of \$10,000.00 enough shall have been provided to cancel it?*

$= 10000 \times (\frac{1}{a_n} - i)$

(*b*) *Show the Journal entry at the time of the first sinking fund installment.*

(*c*) *Show a type entry when investments are bought.*

(*d*) *Show the entry when the mortgage is paid.*

2. (*a*) This problem cannot be answered by students of elementary accounting, because a knowledge of what Professor

Sprague has called the Accountancy of Investment is essential. Students of advanced algebra, however, can easily determine the amount which has to be set aside each year, for fifteen years, so that at the end of the period enough will have been accumulated to cancel the indebtedness of $10,000.00, provided they know the rate of interest which each installment as set aside will earn. The figure may also be obtained by applying the proper formula or by consulting a table which shows how much $1.00 will amount to if set aside at the beginning of each year for a given number of years, if each installment as made, is immediately invested at a fixed rate per cent.

$1.00 invested at the beginning of each year, for fourteen years, at four per cent., compounded annually, amounts to $19.0235. As the last installment draws no interest, only fourteen interest periods should be taken. The total amount will accordingly be $20.0235 per dollar, *i. e.*, for every dollar so set aside, $20.0235 of the $10,000.00 will be canceled. $10,000.00 divided by $20.0235, or $~~449.41~~, is the amount of the annual installment. 499.41

(*b*) (1) Surplus	$449.41	
To Sinking Fund Reserve		$449.41
For the purpose of retaining sufficient profits to meet sinking fund requirements.		
(2) Sinking Fund Cash	449.41	
To Cash		449.41
First installment set aside for the purpose of meeting, at maturity, 15-year mortgage, executed .... (insert date).		
(*c*) Sinking Fund Investments	$———	
To Sinking Fund Cash		$———
Purchased......bonds, at $.........		
(*d*) (1) First Mortgage Bonds Payable	$15,000.00	
To Sinking Fund Cash		$15,000.00
Cancellation of mortgage at maturity. (We assume here that the sinking fund investments have been disposed of previously.)		

(2) Sinking Fund Reserve	$15,000.00	
To Reserve		$15,000.00
Transfer of the Sinking Fund Reserve to ordinary Reserve Account, as there is no longer any valid ground for retaining profits in order to meet bonded indebtedness.		

(Pp. 198–199); S., 31; H., 271–272; G. I, 118–124; G. II, 14–15; D. D., 57–65; R. C., 148–154; W. A., 149–152; J., Vol. 14, 113–116, Vol. 17, 165–176.

3. *As an original exercise, securing such help as you can from the bibliographical list appended to this chapter, find how much each installment should have been if it were immediately invested at 3 per cent.*

3. We shall not show here the method described by Professor Sprague in his Accountancy of Investment. It will suffice to refer to a table which shows how much there will result from depositing $1.00 at the end of each year for fifteen years, if each installment draws interest at 3%, as soon as deposited. $1.00 will amount to $19.1568; dividing $15,000.00 by $19.1568, gives us as the installment necessary to be set aside each year, $783.01.

(See reference to Exercise 2, above.)

4. *Show a type entry for depreciation.*

4 (*a*) If the depreciation is on machinery, the following is a type entry:

Manufacturing Account	$———	
To Machinery Depreciation		$———

(*b*) If the depreciation refers to warehouse fixtures, the following is a type entry:

Trading Account	$———	
To Depreciation on Fixtures		$———

(Pp. 185–186.)

5. *Show a type entry for depreciation reserve.*

5	Surplus	$———	
	To Reserve for Depreciation		$———

(Pp. 192–193.)

SOLUTIONS TO EXERCISES

CHAPTER IX

ADVANCED FORMS OF FINAL STATEMENTS

Group One

1. *Define prime cost.*

1. Prime cost is the name applied to the first division of the Manufacturing Section of the Profit and Loss Statement. This is the cost of the goods or materials actually consumed in the process of manufacturing, plus the freight inward, if any, plus the direct factory wages.

(Pp. 211–212); H., 296.

2. *In terms of the two divisions of the Manufacturing Section where would you place (a) Wages, (b) Fuel, (c) Machinery Depreciation? Give reasons in each case.*

2. (*a*) Wages to Prime Cost, because a *direct* manufacturing charge.
   (*b*) Fuel to Overhead, because an *indirect* manufacturing charge.
   (*c*) Machinery depreciation to Overhead because an *indirect* manufacturing charge.

3. *What is the function of the Appropriation Section?*

3. The Appropriation or Apportionment Section shows how the net profits of a certain period were distributed or how the net loss for the period was taken care of.

(P. 215.)

4. *In submitting a report to the president of a manufacturing company, would you prefer to employ a Profit and Loss*

Account or a Profit and Loss Statement? Give full reasons for your choice.

4. I should prefer to use a Profit and Loss Statement because by means of it the lay reader is enabled to comprehend the knowledge to be presented much better. The Account is a technical form, which is thoroughly understood only by the man trained in bookkeeping and accounting, whereas a statement is just as clear to the trained bookkeeper and accountant, but clearer by far to the ordinary business man.

5. *Write an essay of about three hundred words on Terminology and Forms. Treat of the student's difficulties because of confusions in terminology and non-uniformity.*

5. Every practical subject reflects the whims, caprices, judgments, study and ignorance of those who practice it; just as every living language is constantly changing, so does every practical subject constantly manifest itself in new forms. It is perhaps unfortunate that the beginner in accounting should be confronted with a veritable babel of words and forms, employed by different practitioners, sometimes it would appear without reason. We find in accounting different terms employed to express the same thought and the same thought expressed by different terms. We also find different forms employed to present the same fact, and, worst of all, different names applied to the same forms. Examples are readily available. *On cost, burden* and *overhead* are used to express the same idea. *Cost of sales* sometimes means *selling costs* and sometimes includes *turnover* and *selling costs. Profit and Loss Account* and *Profit and Loss Statement* are frequently used synonymously, but each term should be restricted to a particular form.

(Pp. 195, 206, 234); H., 56.

The fact that an unnecessary difficulty confronts students of accounting due to this confusion in terminology and forms, should add zest to their study, because they should

feel that there is a goal to attain and work to be done. The field is a broad and vast one; it demands the best in a man; and there is hope that every real contribution in the nature of form and terminology standardization will be truly and really appreciated by the great and ever-growing army of brilliant men who are devoting their lives to the service of accounting. In this connection, the final report on standardization by a committee of the American Association of Public Accountants is awaited with interest.

(Pp. 195, 206, 234); H., 56; J., Vol. 9, 275–278, Vol. 10, 201–208, 435–438, Vol. 13, 109–121, 161–181, 315–338, 389–400, Vol. 16, 424–431.

Group Two

1. *Prepare a Profit and Loss and Income Statement from Exercise 1, Group Two, page 69.*

For solution, see page 71. Items should be arranged according to form on page 86, resulting in a net profit of $5,996.50. For additional suggestion as to form see Elements of Accounting, pages 225-228.

2. *From the Trial Balance on page 83—*
   (*a*) *Prepare a Trading and Profit and Loss Statement.*
   (*b*) *Prepare a Profit and Loss and Income Statement.*
   (*c*) *Prepare Journal entries, with full original entry explanations, for a Profit and Loss Account.*
   (*d*) *Prepare a Profit and Loss Account.*
   (*e*) *Prepare a Balance Sheet.*

Inventories as follows:

Raw Materials, $3,600.00; goods in process, $4,500.00; finished goods, $5,800.00. Write off for bad debts, $470.00. Write off $1,000.00 from plant and machinery for depreciation and $200.00 from tools. Eighty dollars of the factory insurance is still in force. Factory wages accrued amount to $120.00. Reserve $2,000.00, and declare dividends of 6% on the preferred stock, and of 10% on the common stock.

Trial Balance of the Kent Mfg. Co.

December 31, 1913

Preferred Capital Stock		$10,000.00
Common Capital Stock		10,000.00
Unsubscribed Common Capital Stock	$2,500.00	
Cash	3,800.00	
Notes Receivable	6,750.00	
Accounts Receivable	12,000.00	
Loans Payable		5,000.00
Accounts Payable		8,750.00
Plant and Machinery	10,000.00	
Depreciation on Plant		2,000.00
Factory Tools	500.00	
Raw Materials 1/1/13	3,000.00	
Purchases	20,000.00	
Returned Purchases		1,000.00
Sales		57,770.00
Sales Returns	1,200.00	
Discount on Purchases		175.00
Discount on Sales	310.00	
Wages	8,200.00	
Factory Insurance	150.00	
Factory Expense	1,300.00	
Fuel	2,200.00	
Factory Salary	3,200.00	
Freight Outward	1,100.00	
Finished Goods 1/1/13	4,000.00	
Selling Expenses	7,300.00	
Commission	1,800.00	
Office Expense	2,150.00	
Office Salary	4,000.00	
Discount	165.00	
Interest on Loans	300.00	
Reserve		1,000.00
Surplus		230.00
	$95,925.00	$95,925.00

2 (*a*)

Trading and Profit and Loss Statement of the Kent Manufacturing Company

FOR THE PERIOD ENDED DECEMBER 31, 1913

MANUFACTURING SECTION

Raw Materials (1/1/13)		$3,000.00	
Purchases		20,000.00	$23,000.00
Less Returned Purchases		$1,000.00	
Raw Material (12/31/13)		3,600.00	
Goods in Process (12/31/13)		4,500.00	9,100.00
COST OF GOODS CONSUMED			$13,900.00
Wages		$8,200.00	
Accrued		120.00	8,320.00
PRIME COST			$22,220.00
Factory Insurance	$150.00		
Less Unconsumed	80.00	$70.00	
Factory Expense		1,300.00	
Fuel		2,200.00	
Factory Salary		3,200.00	
Depreciation on Plant and Machinery		1,000.00	
Depreciation on Tools		200.00	
FACTORY OVERHEAD			7,970.00
			$30,190.00

Manufacturing Cost, being cost of Manufacturing for the year, carried to Trading Section	$30,190.00
	$30,190.00

TRADING SECTION

Manufacturing Cost, brought down from Manufacturing Section	$30,190.00	
Finished Goods (1/1/13)	4,000.00	$34,190.00
Less Finished Goods (12/31/13)		5,800.00
TURNOVER		$28,390.00
Freight Outward	$1,100.00	
Selling Expenses	7,300.00	
Commission	1,800.00	
SELLING EXPENSES		10,200.00
		$38,590.00
Gross Profit on Trading carried to Administration Section		17,670.00
		$56,260.00

Sales		$57,770.00	
Less Returned Sales	$1,200.00		
Discount on Sales	310.00	$1,510.00	
NET SALES			$56,260.00
			$56,260.00

ADMINISTRATION SECTION

Office Expense	$2,150.00		Gross Profit on Trading, brought down from Trading Section	$17,670.00
Office Salary	4,000.00			
COST OF ADMINISTRATION		$6,150.00		
Gross Business Profit, carried to Profit and Loss Section		11,520.00		
		$17,670.00		$17,670.00

PROFIT AND LOSS SECTION

Discount	$165.00		Gross Business Profit brought down from Administration Section	$11,520.00
Bad Debts	470.00		Discount on Purchases	175.00
Interest on Loans	300.00	$935.00		
Net Business Profit, carried to Appropriation Section		10,760.00		
		$11,695.00		$11,695.00

APPROPRIATION SECTION

Reserve	$2,000.00		Net Business Profit brought down from Profit and Loss Statement	$10,760.00
Dividends Payable	1,350.00	$3,350.00		
Surplus		7,410.00		
		$10,760.00		$10,760.00

(Pp. 212–217); G. I., 89–90, 113; G. II., 11–13.

(*b*)

Profit and Loss and Income Statement of the Kent Manufacturing Company

FOR THE PERIOD ENDED DECEMBER 31, 1913

Sales			$57,770.00
Less Returned Sales		$1,200.00	
Discount on Sales		310.00	1,510.00
NET SALES			$56,260.00
Deduct Cost of Manufacturing:			
Prime Cost:			
Raw Materials (1/1/13)		$3,000.00	
Purchases		20,000.00	
Wages (including accrued $120.00)		8,320.00	
		$31,320.00	
Less Returned Purchases	$1,000.00		
Inventory Raw Mat. (12/31/13)	3,600.00		
Inventory Goods in Process (")	4,500.00	9,100.00	
PRIME COST		$22,220.00	
Factory Overhead:			
Fuel	$2,200.00		
Factory Salary	3,200.00		
Depreciation on Plant and Mach.	1,000.00		
Depreciation on Tools	200.00		
Factory Insurance	70.00		
Factory Expense	1,300.00		
FACTORY OVERHEAD		7,970.00	
Cost of Year's Manufacturing		$30,190.00	
Add Inv. of Finished Goods (1/1/13)		4,000.00	
		$34,190.00	
Less Inv. of Finished Goods (12/31/13)		5,800.00	
Manufacturing Cost of Sales for Year			28,390.00
GROSS PROFIT OF SALES			$27,870.00
Deduct Selling and Administration Expenses:			
Freight Outward		$1,100.00	
Selling Expenses		7,300.00	
Commission		1,800.00	
Office Expense		2,150.00	
Office Salary		4,000.00	
COST OF SELLING AND ADMINISTRATION			$16,350.00
GROSS BUSINESS PROFIT			$11,520.00
Deduct:			
Discount on Notes		$185.00	
Interest on Loans		300.00	
Bad Debts		470.00	935.00
			$10,585.00
Add Discount on Purchases			175.00
NET BUSINESS PROFIT			$10,760.00
Distributed as follows:			
Reserve		$2,000.00	
Dividends Payable		1,350.00	3,350.00
CARRIED TO SURPLUS			$7,410.00

(Pp. 225–228); G. II, 66–68, 150–152; H., 280–282; M., 228–229.

December 31, 1913

(c)

Purchases	$3,000.00	
To Raw Materials Inventory (1/1/13)		$3,000.00
To transfer Raw Material Inventory to Purchases Account and to close the former account.		
31		
Returned Purchases	1,000.00	
Raw Materials Inventory	3,600.00	
Goods in Process	4,500.00	
To Purchases		9,100.00
To obtain cost of goods consumed, to close Returned Purchases Account and to open Raw Materials Inventory and Goods in Process Accounts.		
31		
Manufacturing Account	13,900.00	
To Purchases		13,900.00
To transfer cost of goods consumed to Manufacturing Account and to close the Purchases Account.		
31		
Wages	120.00	
To Wages Accrued		120.00
To obtain real cost of Factory Labor and to open Wages Accrued Account.		
31		
Unexpired Factory Insurance	80.00	
To Factory Insurance		80.00
To set up Unexpired Factory Insurance and to obtain real cost of Factory Insurance for the year.		
31		
Manufacturing Account	16,290.00	
To Wages		8,320.00
Factory Insurance		70.00
Factory Expenses		1,300.00
Fuel		2,200.00
Factory Salary		3,200.00
Depreciation on Plant and Machinery		1,000.00
Tools		200.00
To obtain Manufacturing Cost for year.		

31		
Trading Account	$30,190.00	
To Manufacturing Account		$30,190.00
To transfer Manufacturing Cost for year to Trading Account and to close Manufacturing Account.		
31		
Trading Account	4,000.00	
To Finished Goods (1/1/13)		4,000.00
To transfer Finished Goods Inventory to Trading Account and to close the former account.		
31		
Finished Goods Inventory	5,800.00	
To Trading Account		5,800.00
To open new Inventory Account.		
31		
Trading Account	10,200.00	
To Freight Outward		1,100.00
Selling Expenses		7,300.00
Commission		1,800.00
To transfer Selling Expenses to Trading Account.		
31		
Sales	1,510.00	
To Returned Sales		1,200.00
Discount on Sales		310.00
To obtain Net Sales and to close Returned Sales Account and Discount on Sales Accounts.		
31		
Sales	56,260.00	
To Trading Account		56,260.00
To close Sales into Trading Account.		
31		
Trading Account	17,670.00	
To Administration Account		17,670.00
To transfer Gross Profit on Trading to Administrative Account and to close Trading Account.		

31

Administration Account	$6,150.00	
To Office Expense		$2,150.00
Office Salary		4,000.00

To transfer Costs of Administration to Administration Account.

31

Administration Account	11,520.00	
To Profit and Loss Account		11,520.00

To transfer Gross Business Profit to Profit and Loss Account and to close Administration Account

31

Bad Debts	470.00	
To Accounts Receivable		470.00

To open up Bad Debts Account and to deduct from Accounts Receivable.

31

Profit and Loss Account	935.00	
To Bad Debts		470.00
Discount		165.00
Interest on Loans		300.00

To transfer losses shown by credit items to Profit and Loss Account.

31

Discount on Purchases	175.00	
To Profit and Loss Account		175.00

To close Discount on Purchases into Profit and Loss Account.

31

Profit and Loss Account	10,760.00	
To Appropriation Account		10,760.00

To transfer Net Business Profit to Appropriation Account and to close Profit and Loss Account.

31

Appropriation Account	10,760.00	
To Reserve		2,000.00
Dividends Payable		1,350.00
Surplus		7,410.00

To close Appropriation Account.

(Pp. 176–178, 219–222); G. I, 44.

(*d*)

MANUFACTURING ACCOUNT

1913			1913		
Dec. 31	J 1	$13,900.00	Dec. 31	J 2	$30,190.00
	J 1	16,290.00			
		$30,190.00			$30,190.00

TRADING ACCOUNT

1913			1913		
Dec. 31	J 2	$30,190.00	Dec. 31	J 2	$5,800.00
	J 2	4,000.00		J 2	56,260.00
	J 2	10,200.00			
	J 2	17,670.00			
		$62,060.00			$62,060.00

ADMINISTRATION ACCOUNT

1913			1913		
Dec. 31	J 3	$6,150.00	Dec. 31	J 2	$17,670.00
	J 3	11,520.00			
		$17,670.00			$17,670.00

PROFIT AND LOSS ACCOUNT

1913			1913		
Dec. 31	J 3	$936.00	Dec. 31	J 3	$11,520.00
	J 3	10,760.00		J 3	175.00
		$11,695.00			$11,695.00

APPROPRIATION ACCOUNT

1913			1913		
Dec. 31	J 3	$10,760.00	Dec. 31	J 3	$10,760.00

(Pp. 222–225); G. I, 45, 126–128; G. II, 50–53, 122–123; H., 276–277, 279, 284, 285; L., 54–58, 60–63.

3. *Show the Balance Sheet after all the dividends, except those on fifteen shares of common stock, have been paid.*

2 (*e*) and 3.

Balance Sheet of the Kent Manufacturing Company

DECEMBER 31, 1913

Cash *		$3,800.00	
Accts. Rec.	$12,000.00		
Less Bad Debts written off	470.00	11,530.00	
Notes Rec.		6,750.00	$22,080.00
Unexpired Factory Insurance			80.00
Raw Materials		$3,600.00	
Goods in Process		4,500.00	
Finished Goods		5,800.00	13,900.00
Plant and Machinery	$10,000.00		
Less Depreciation	3,000.00	$7,000.00	
Tools	$500.00		
Less Depreciation	200.00	300.00	7,300.00
			$43,360.00

Loans Payable		$5,000.00	
Accts. Pay.		8,750.00	
			$13,750.00
Wages Accrued			120.00
Dividends Pay.*			1,350.00
			$15,220.00
Capital:			
Pref. Cap. Stock		$10,000.00	
Com. Cap. Stock	$10,000.00		
Less Unsubscribed Stock	2,500.00	7,500.00	
Reserve	$1,000.00		
Current	2,000.00	3,000.00	
Surplus	$230.00		
Current	7,410.00	7,640.00	28,140.00
			$43,360.00

(Pp. 217–218); G. II, 69, 124, 134; H., 59–68; M., 212–223; E., 432–439.

* These items are correct for the Solution to 2 (*e*). For Exercise 3, change Cash to $2,600.00 and Dividends Payable (Unpaid Dividends) to $150.00.

SOLUTIONS TO EXERCISES

CHAPTER X

ACCOUNTS OF NON-TRADING CONCERNS

Group One

1. *Define Statement of Receipts and Disbursements.*

1. A Statement of Receipts and Disbursements is a summary cash statement of a non-trading concern, showing the amount of cash on hand at the beginning of period, if any, to which is added the actual receipts of cash for the period, under appropriate headings, from all of which is deducted the disbursements of the period, properly recapitulated, and resulting in the balance of cash on hand at the end of the period.

(Pp. 242, 245–246.)

2. *Define Revenue Account.*

2. Revenue Account is synonymous with the Statement of Income and Expenditures or the Statement of Income and Expenses. It is a summary profit and loss statement of a non-trading concern, corresponding to the Profit and Loss Statement of an ordinary concern, so arranged as to recapitulate, under proper captions, all the income applicable to the period under review, *whether actually* received or not, and also a similar arrangement of the expenses for the period, *whether actually paid or not,* and resulting in the CURRENT REVENUE SURPLUS OR CURRENT REVENUE DEFICIT.

(Pp. 238–239.)

3. *Differentiate between an Income and Expenditure Account and a Receipts and Payments Account.* ([illegible])

3. The difference between an Income and Expenditure Account and a Receipts and Payments Account, is that the former refers to income and expense items, whereas the latter refers to cash items. The income for a period may or may not be equal to the cash received during the period; the expenses for a period may or may not be equal to the cash disbursed during the period. In one case, and in only one case, are the two accounts or statements identical. This occurs when there was no cash balance at the beginning of the period and when all the cash received for the period was for current income and all the current income was received in cash, and when all the expenses for the period were paid in cash and no expenses were prepaid; and when, moreover, none of the receipts of cash for the period were in the nature of payments from a past period, and when none of the disbursements of cash for the period were in payment of expenses incurred in the previous period. Only under such an unusual set of circumstances would the two statements or accounts be identical. In practically every instance, however, the two statements are different and both must be prepared.

(P. 243.)

4. *What is the function of a Balance Sheet in a non-trading concern?*

4. The function of the Balance Sheet of a non-trading concern is the same as the function in any kind of concern. It is to show the various assets on one side and the various liabilities on the other. If the assets are greater than the liabilities, there is a capital surplus; in the reverse case there is a capital deficit.

(Pp. 160–161.)

5. *Discuss the importance of observing the distinction between capital and revenue when applied to the accounting system of a hospital.*

5. It is always important to observe the distinction between capital and revenue. The student will recall the evil results following from failure to observe this distinction as pointed out in Elements of Accounting, pages 21-23. To apply the points specifically to the accounting system of a hospital, failure to charge repairs and maintenance of buildings to proper expense or revenue accounts, *i. e.,* to charge such items to Construction or Real Estate or Building Account, would be to lead the directors and patrons of the institute to believe that operations were being conducted at a lower figure than was really the case. Thus at the end of a number of years it would be found that the property of the hospital, upon appraisal, was much less than that shown by the books. Other examples can easily be produced.

(Pp. 21–23); H., 72–74; M., 203; J., Vol. 4, 167–184, 247–260.

6. *Draw up a* pro forma (*items with figures omitted*) *Statement of Income and Expenses and a Statement of Receipts and Payments for any society with whose books you are familiar.*

6. This is an original proposition which each student must answer for himself. Those who have had no experience whatsoever can not, of course, produce the desired statement, and it would serve no purpose to present one. However, it may be said in passing, that the Statement of Income and Expenses of the A.D. Medical Society, page 251, Elements of Accounting, with *all* figures omitted, would be a sufficient answer to the first part of the question. The Statement of Receipts and Disbursements of the same Society, page 252, Elements of Accounting, with *all* figures similarly omitted, would be a sufficient answer to the second part of this question.

Group Two

1. *Complete the following Trial Balance, and from it and the supplementary data prepare the usual Statements:*

Trial Balance of the ______________ Society

December 31, 1913

L.F.		Dr.	Cr.	1913 Transactions Dr.	1913 Transactions Cr.	December 31, 1913 Dr.	December 31, 1913 Cr.
	Cash	$3,510.00		$6,196.00	$3,093.00		
	Dues Receivable	1,040.00		5,600.00	6,100.00		
	Dues				5,600.00		
	Library	1,200.00		400.00	30.00		
	Library Expense			310.00			
	Secretary's Office			200.00			
	Postage			175.00			
	Investments	10,000.00					
	Collection and Exchange			8.00			
	Furniture	3,000.00		1,600.00			
	Telephone			300.00	16.00		
	Interest				50.00		
	Accounts Payable		500.00	1,900.00	1,800.00		
	Surplus		18,250.00				
		$18,750.00	$18,750.00	$16,689.00	$16,689.00		

The following bills have not been entered:

New York Telephone Co.	*$45.00*
Repairs to Library	*37.00*

It is decided to cancel dues amounting to $160.00, because of financial inability on the part of some members. A donation of $1,000.00 worth of books, made on December 31, 1913, has not been entered.

1. **Trial Balance of the ———————— Society**

DECEMBER 31, 1913

Cash	$6,613.00	Dues	$5,600.00
Dues Receivable	540.00	Interest	50.00
Library	1,570.00	Accounts Payable	400.00
Library Expense	310.00	Surplus	18,250.00
Secretary's Office	200.00		
Postage	175.00		
Investments	10,000.00		
Collection and Exchange	8.00		
Furniture	4,600.00		
Telephone	284.00		
	$24,300.00		$24,300.00

Statement of Receipts and Disbursements of the ———————— Society

FOR THE YEAR ENDED DECEMBER 31, 1913

Cash on hand January 1, 1913		$3,510.00
RECEIPTS		
Dues Received	$6,100.00	
Library	30.00	
Telephone	16.00	
Interest	50.00	6,196.00
		$9,706.00
DISBURSEMENTS		
Library	$400.00	
Library Expense	310.00	
Postage	175.00	
Collection and Exchange	8.00	
Telephone	300.00	
Accounts Payable	1,900.00	
		$3,093.00
Balance		$6,613.00

Statement of Income and Expenses of the ——————— Society

FOR THE YEAR ENDED DECEMBER 31, 1913

INCOME			
Dues		$5,600.00	
Interest		50.00	
Telephone		16.00	
Total Income			$5,666.00
EXPENSES			
Telephone	$300.00		
Plus Accrued	45.00	$345.00	
Library Expense	$310.00		
Repairs to Library	37.00	347.00	
Secretary's Office		200.00	
Postage		175.00	
Collection and Exchange		8.00	
Total Expenses			1,075.00
Current Revenue Surplus			$4,591.00
CAPITAL SURPLUS			
Old Balance			$18,250.00
Library Donation	$1,000.00		
Current Revenue Surplus	4,591.00	$5,591.00	
Less Dues Canceled		160.00	
			5,431.00
Capital Surplus			$23,681.00

Balance Sheet

Cash	$6,613.00	Accounts Payable	$482.00
Dues Receivable	380.00	Capital Surplus	23,681.00
Investments	10,000.00		
Library	2,570.00		
Furniture	4,600.00		
	$24,163.00		$24,163.00

(Pp. 248–254.)

2. *Express your opinion as to the financial condition of this society.*

2. The .... Society appears to be in a very healthy condition. This is shown by the fact that the income for the year amounted to over $5,000.00, while the total expenses for the year were only $1,000.00, so that the excess of income over expenses was over $4,000.00. The annual dues exceed the running expenses by a large margin. The Balance Sheet shows, also, that the current assets are much in excess of all current liabilities, so that the Society is upon an excellent working basis.

SOLUTIONS TO EXERCISES

CHAPTER XI

STATEMENT OF AFFAIRS AND DEFICIENCY ACCOUNTS

Group One

1. *Clearly distinguish (a) Statement of Assets and Liabilities, (b) Balance Sheet, (c) Statement of Affairs.*

1. (*a*) The Statement of Assets and Liabilities is a statement prepared from Double Entry books, or Single Entry books, plus information obtained from outside sources; or, it is prepared without the aid of books at all. Its purpose is to show on one side all of the values belonging to the business; on the other side all that the business is liable for. The Assets and Liabilities are grouped under appropriate headings. The difference between the Assets and the Liabilities is called NET WORTH OR NET CAPITAL, if the Assets exceed the Liabilities, or NET DEFICIT, if the Liabilities exceed the Assets.

(*b*) The Balance Sheet corresponds to the Statement of Assets and Liabilities, but it is always made up (technically) from Double Entry Books, in balance, after the books have been closed. After closing Double Entry books it will be found that all the balances which still exist are either assets or liabilities, or balances representing proprietorship. If these items are properly separated and grouped, a modern Balance Sheet results.

(*c*) The Statement of Affairs corresponds to the Statement of Assets and Liabilities. The difference is this: whereas the Statement of Assets and Liabilities is prepared for a solvent

concern, the Statement of Affairs is the Financial Statement which is prepared for an insolvent concern or a concern temporarily embarrassed. The latter consists of two asset columns and two liability columns. One asset column is for book values, while the other shows how much may be expected from such assets, upon realization; the first of the liability columns shows the book value of liabilities, while the second one shows the amounts which will have to be paid to liquidate such liabilities. The difference between the second asset column and the second liability column gives the deficiency, the amount which cannot be paid to general creditors.*

(P. 258); H., 335; G. II, 186, 187–188; E., 461–463.

2. *What is the function of a Statement of Affairs?*

2. The function of the Statement of Affairs has already been indicated in the answer to "c," above. Its function is to show what general unsecured creditors may expect to receive from the concern. This amount, as indicated by the second asset column, constitutes their dividend. The dividend is sometimes expressed as so many "cents on the dollar." Thus, if general unsecured creditors amount to $5,000.00, while the second asset column shows $3,000.00, creditors may expect a dividend of sixty cents on the dollar, *i. e.,* $3,000.00 divided by $5,000.00, or 60%.

See references for Exercise 1, above.

3. *Define Deficiency Account.*

3. The Deficiency Account almost invariably follows the Statement of Affairs. It is at once the reason and the excuse for the Statement of Affairs, for it shows why creditors cannot be paid in full. It shows on one side the losses of past periods, current trade losses, plus shrinkages due to forced

* This statement is not universal. Some exceptions occur.

realization, plus drawings or dividends of proprietors. On the other side will be found the original investments, plus profits during past periods, plus the deficiency. This Deficiency must correspond to the Deficiency shown in the Statement of Affairs.

(Pp. 266–267); H., 335.

4. *Who constitute preferred creditors? How are they shown on the Statement of Affairs?*

4. Preferred creditors are made preferred by statute. In general, they constitute the claims of the state or other public body for taxes, and the claims of workers for wages and salaries. In New York City, the order of preference is as follows:

Claims of the United States; claims of the State; claims of the City (County and City of New York are synonymous); wages and salaries.

Each class must be paid in full before the next class of lesser preference is paid at all; and all preferred claims must be met before general creditors are given anything.

Preferred creditors are shown in the "Nominal" or "Book Value" column on the liability side of the Statement of Affairs, but they are *not* extended into the "To Rank" column. Instead of so extending them, they are deducted from the second, or "Expected to Realize" column, on the asset side of the Statement of Affairs.

(P. 263; E., 473.)

5. *What is meant by "creditors fully secured"? By "creditors partially secured"?*

5. "Creditors fully secured" constitute such creditors as hold security for the repayment of debts, at least equal in value to the amount of the indebtedness. In general, they include such creditors as banks that lend on notes secured by col-

lateral, holders of mortgages against property, financiers who make advances on chattel mortgages, or on other security. They are said to be fully secured only when the value of the collateral or security held by them is at least sufficient to pay the full amount of the debt due them.

"Creditors partially secured" constitute a similar class of creditors, but the difference between them and the "fully secured creditors" lies in the fact that the security which the "partially secured creditors" hold will not be sufficient to cancel the full indebtedness to them. For that portion of the debt which the sale of the security will not liquidate, they become general creditors.

On the liability side "fully secured creditors" are not shown in the "Expected to Rank" column, but only in the "Gross" column; "partially secured creditors" have the full amount of their claims in the "Nominal" column, but only that portion of their claims which will not be canceled by the securities which they hold, is extended into the second, or "Expected to Rank" column.

(Although not asked for in this question, it is well to remember that the securities held by creditors, while shown in the first asset column, are not extended into the second asset column, except for such portion as will remain over after fully secured creditors have been paid their claims.)

(P. 266.)

6. *How can the accountant know what the book assets will produce when sacrificed?*

6. As a matter of fact, he cannot know definitely and positively. It must be confessed that the amount shown is, after all, a more or less scientific guess. The amounts are often determined as a result of the combined efforts of the accountant, the proprietor, some of the creditors and experts.

7. *What is the relationship between the Statement of Affairs and the Deficiency Account?*

7. This question has been answered, practically, in the answer to Exercise 3, above. The answer may be recapitulated as follows: While the Statement of Affairs lists the individual assets and the individual liabilities, and results in the *deficiency,** the amount which cannot be liquidated, the Deficiency Account attempts to account for or explain the deficiency.

Group Two

1. *Prepare a Statement of Affairs and a Deficiency Account for Mr. Black, whose Balance Sheet is shown on page 162.† He has been in business two years, for which period his net loss has been $1,800.00. He commenced with a capital of $8,000.00, and his drawings during the past two years amounted to $1,200.00. You are informed that his Accounts Receivable are all good. Accounts Payable include taxes amounting to $600.00. Upon a forced sale, it is expected that the goods on hand will bring $2,200.00, real estate $2,500.00, and machinery $3,500.00.*

(Solution on page 104.)

2. *Prepare a Statement of Affairs and a Deficiency Account on the basis of the data furnished by Exercise 1, Group Two, page 69. Assume the following facts: (a) Merchandise will probably bring $4,100.00; (b) Office furniture, $325.00; (c) Accounts receivable consist of $4,300.00 good debts, $2,500.00 doubtful, estimated to be worth 60%, balance bad; (d) Notes Receivable are all good.*

(Solution on page 105.)

* This statement is not universal. Some exceptions occur.

† Reference to Elements of Accounting.

1. (Question on page 103.)

Statement of Affairs of B. B. Black

APRIL 1, 1913

Nominal Value	Assets	Expected to Realise	Nominal Value	Liabilities	Expected to Rank
$1,200.00	Cash	$1,200.00	$4,500.00	Notes Payable	$4,500.00
2,000.00	Accounts Receivable	2,000.00	7,600.00	Accounts Payable	7,600.00
3,000.00	Merchandise	2,200.00	600.00	Preferred Creditors (Taxes)	
9,000.00	Machinery	3,500.00			
2,500.00	Real Estate	2,500.00	$12,700.00		
$17,700.06		$11,400.00			
	Less Preferred Creditors as *per contra*	600.00			
		$10,800.00			
	Deficiency	1,300.00			
		$12,100.00			$12,100.00

Deficiency Account

Investment	$8,000.00	Net loss during the past two years		$1,800.00
Deficiency	1,300.00	Shrinkages as per Statement of Affairs:		6,300.00
		Merchandise	$800.00	
		Machinery	5,500.00	
		Drawings		1,200.00
	$9,300.00			$9,300.00

See references for the next exercise.

2. (Question on page 103.)

Statement of Affairs of Topper & Hinds

APRIL 1, 1913

Nominal Value	Assets		Expected to Realize	Nominal Value	Liabilities		Expected to Rank
$4,376.50	Cash		$4,376.50	$2,500.00	Notes Payable		$2,500.00
4,000.00	Notes Receivable		4,000.00	3,950.00	Accounts Payable		3,950.00
7,000.00	Accounts Receivable:			310.00	Preferred Creditors deducted from Assets as *per contra*		
	Good	$4,300.00	4,300.00		Wages	$310.00	
	Doubtful	2,500.00	1,500.00				
	Bad	200.00					
6,280.00	Merchandise		4,100.00				
800.00	Furniture		325.00				
				$6,760.00			$6,450.00
100.00	Prepaid Rent		$18,601.50				
$22,556.50	*Less* Preferred Creditors as *per contra*		310.00		Balance to be divided between partners		11,841.50
			$18,291.50				$18,291.50

Deficiency Account

Investment	**$10,000.00**	**Shrinkages as per Statement of Affairs:**		**$3,955.00**
Profits	**5,996.50**	**Accounts Receivable**	**$1,200.00**	
		Merchandise	**2,180.00**	
		Furniture	**475.00**	
		Rent	**100.00**	
		Drawings		**200.00**
		Balance		**11,841.50**
	$15,996.50			**$15,996.50**

(Pp. 269–274); H., 335–340; G. A., 408–420; G. I, 65–68, 108–110, 116–117, 137–139; L., 82–92; E., 466–472.

SOLUTIONS TO EXERCISES

CHAPTER XII

REALIZATION AND LIQUIDATION

Group One

1. *What is a Realization and Liquidation Account?*

1. A Realization and Liquidation Account is prepared from the books of a receiver or trustee to show, among other things, the result of such receiver's or trustee's operations. It commences with the assets given to the trustee or receiver to realize upon, usually at their book or nominal values, but not including cash, and opposite these asset items are arranged the corresponding liabilities which are to be liquidated. In both cases the items are arranged somewhat after the fashion of the Trial Balance or Balance Sheet. The assets as realized are then shown *beneath* the liabilities first shown; the liabilities liquidated are similarly shown beneath the assets first listed. The expenses are also shown beneath the assets first listed and after the liabilities liquidated. The loss on realization is shown on the right-hand side, after the manner employed in the realization and liquidation account shown on page 285 of Elements of Accounting.

(P. 278); E., 474–476.

2. *By whom is this account prepared, and for what purpose?*

2. This account, which is really a statement, is prepared by the accountant for the receiver or trustee, for the purpose explained in the answer to question one, above. It might be

well to state that the technical Realization and Liquidation Account, sometimes found in the ledger of the receiver or trustee, and which is a sort of controlling account of the receiver's or trustee's books, is *not* the realization and liquidation account submitted by the receiver or trustee.

(Pp. 287–288.)

3. *To what compensation is a receiver entitled for his services?*

3. In New York State the receiver is entitled to the fees on the amount which he receives and disburses, as follows:

5 %	on the first	$1,000.00,
2½%	on the next	10,000.00,
1 %	on all above	11,000.00.

It should also be noted that the maximum allowance is three fees, so that if five men should act as receivers they would have to divide among themselves three fees.

(P. 285–286); G. II, 162, 199.

4. *Point out the difference between the Summary Cash Account and the Realization and Liquidation Account. What information do they contain in common? What information cannot be found in both, but only in one or the other?*

4. The difference between the Summary Cash Account and the Realization and Liquidation Account is somewhat similar to the difference between the Statement of Receipts and Disbursements and the Income and Expense Statement of non-trading concerns. The Summary Cash Account commences with the balance of the cash at beginning, to which is added the cash receipts under appropriate headings. From the sum of the receipts and original balance there is deducted the disbursements, also under appropriate headings. The Realization and Liquidation Account has already been explained in the answer to question one.

Both of these accounts have something in common—they both refer to the same enterprise; they are both prepared from

the same set of books; they are both parts of the same report; but while the Realization and Liquidation Statement shows the loss or gain, the cash account shows the balance of cash on hand, if any. Some information is found in but one of the two statements: for example, the cash balance is found in the cash statement only; loss on operations is found in the Realization and Liquidation Statement only.

5. *Why are the affairs of a concern temporarily embarrassed sometimes taken in charge by a creditors' committee? Describe what you believe to be the functions of such a committee.*

5. The affairs of such a concern are sometimes taken over by a creditors' committee for the purpose of conserving the interest of the creditors and for the purpose of rehabilitating the concern or keeping in business a good customer. The function of such a committee is to remain in charge of the affairs only until such a time as the concern no longer needs outside help, *i. e.*, until the crisis has been passed. The committee should conduct the affairs most economically; it should not incur any debts unless absolutely necessary; it should encourage creditors to extend additional time, and it should do all in its power to safeguard the interests of the proprietors of the concern, without, however, jeopardizing the interest of creditors, for it must never be forgotten that the primary function of the committee is to look after the interest of the creditors. Incidentally, it must be observed that the members of the creditors' committee must not give preference to their own individual claims.

Group Two

1. *To how much fee is a receiver entitled who winds up a business, the assets of which produced $29,674.00, all of which was disbursed, including his own fee?*

5 % on $1,000.00	$50.00
2½% on 10,000.00	250.00
1 % on 18,674.00	186.74
Total	$486.74

(Pp. 285–286.)

2. *Show the Journal entries on the books of the trustee for the transactions involved in the problem on page 280, section II, of* Elements of Accounting.

2. (The following are the complete entries for the operations of the Trustee. The Trustee's statements (accounts) are based upon the resulting ledger accounts. It is assumed, for the sake of convenience, that no Cash Book is employed.)

(1)	Trustee's Summary Cash Account		$3,800.00	
	Realization and Liquidation Account		38,575.00	
	To M., Trustee			$42,375.00
	Assets in hands of Trustee, besides cash, for realization:			
	*Accounts Receivable	$16,410.00		
	Notes Receivable	8,900.00		
	Merchandise	10,000.00		
	Fixtures	3,265.00		
(2)	M., Trustee		$18,675.00	
	To Realization and Liquidation Account			$18,675.00
	Liabilities to be liquidated by Trustee:			
	Notes Payable	$10,000.00		
	Accounts Payable	8,675.00		
(3)	Trustee's Summary Cash Account		$15,385.00	
	Trustee's Profit and Loss Account		1,025.00	
	To Realization and Liquidation Account			$16,410.00

*(Individual items are to be posted.)

	Loss on realization of Accounts Receivable:				
	Book value		$16,410.00		
	Cash Received		15,385.00		
	Loss		$1,025.00		
(4)	Trustee's Summary Cash Account			$7,900.00	
	To Realization and Liquidation Account				$7,900.00
	Notes Receivable Paid		$7,900.00		
(5)	Trustee's Summary Cash Account			$11,250.00	
	Trustee's Profit and Loss Account			2,015.00	
	To Realization and Liquidation Account				$13,265.00
	Loss on realization, as follows:				
	Mdse, Book Value	$10,000.00			
	Cash Received	8,750.00			
	Loss		$1,250.00		
	Fixtures, Book Value	$3,265.00			
	Cash Received	2,500.00			
	Loss		765.00		
	Total Loss		$2,015.00		
(6)	Realization and Liquidation Account			$18,675.00	
	To Trustee's Summary Cash Account				$16,875.00
	Trustee's Profit and Loss Account				1,800.00
	Profit resulting from liquidation, as follows:				
	Accounts and Notes Payable, Book Value		$18,675.00		
	Cash Paid		16,875.00		
	Balance Unpaid (Profit)		$1,800.00		
(7)	Trustee's Expense Account			$335.00	
	To Trustee's Summary Cash Account				$335.00
	Expenses of trustee paid.				

(8)	Trustee's Profit and Loss Account	$335.00	
	To Trustee's Expense Account		$335.00
	To close Trustee's Expense Account.		
(9)	M., Trustee	$1,575.00	
	To Trustee's Profit and Loss Account		$1,575.00
	To close the Profit and Loss Account.		
(10)	M., Trustee	$22,125.00	
	To Mr. L.		$11,712.50
	Mr. M.		10,412.50

To close the Trustee's Account by transferring to Messrs. L. & M. their respective shares of the net assets:

Mr. L.'s Old Capital Balance	$12,500.00
Less ½ Net Loss	787.50
Net Capital Balance	$11,712.50
Mr. M.'s Old Capital Balance	$11,200.00
Less ½ Net Loss	787.50
Net Capital Balance	$10,412.50

(11)	Mr. L.	$11,712.50	
	Mr. M.	10,412.50	
	To Trustee's Summary Cash Account		$21,125.00
	Realization and Liquidation Account		1,000.00

Paid Messrs. L. & M., in full as follows:

Mr. L., Cash	$11,712.50
Mr. M., Cash	$9,412.50
Note	1,000.00
Total	$10,412.50

(Pp. 278–279); G. II, 108–110.

3. *Prepare a Realization and Liquidation Account, a Summary Cash Account, and a Balance Sheet for the liquidation committee which has been winding up the affairs of Topper & Hinds (See page 103, Exercise 2).*

Take into consideration the following facts:

(*a*) *Merchandise brought $5,500.00.*
(*b*) *Furniture was sold for $600.00.*
(*c*) *$1,200.00 was lost on Accounts Receivable.*
(*d*) *Accounts Payable were settled for $3,600.00.*
(*e*) *All other accounts were as shown.*
(*f*) *Expense of winding up was $1,050.00.*

3.

Realization and Liquidation Account of the Firm of Topper & Hinds

APRIL 1, 1913

Assets to be realized:			*Liabilities to be liquidated:*		
Accts. Rec.	$7,000.00		Accts. Pay.	$3,800.00	
Prepaid Rent*	100.00		Notes Pay.	2,500.00	
Notes Rec.	4,000.00		Attorney's Fees	150.00	
Merchandise	6,280.00		Pay Roll Accrued	310.00	
Office Fixtures	800.00	$18,180.00			$6,760.00
Liabilities liquidated:			*Assets realized:*		
Accts. Pay.	$3,600.00		Accts. Rec.	$5,800.00	
Notes Pay.	2,500.00		Notes Rec.	4,000.00	
Attorney's Fees	150.00		Merchandise	5,500.00	
Pay Roll Accrued	310.00	$6,560.00	Office Furniture	600.00	$15,900.00
Realization and Liquidation Expenses		$1,050.00	Net loss due to liquidation		$3,130.00
		$25,790.00			$25,790.00

Summary Cash Account

Balance at beginning	$4,376.50	Accounts Payable	$3,600.00
Accounts Receivable	5,800.00	Notes Payable	2,500.00
Notes Receivable	4,000.00	Attorney's Fees	150.00
Merchandise	5,500.00	Pay Roll Accrued	310.00
Office Fixtures	600.00	Expenses	1,050.00
		Balance	12,666.50
	$20,276.50		$20,276.50

Balance Sheet of Topper & Hinds

AS OF APRIL 1, 1913

Cash	$12,666.50	Wm. L. Topper	$7,798.25	
		Less loss	1,565.00	$6,233.25
		Geo. F. Hinds	$7,998.25	
		Less loss	1,565.00	6,433.25
	$12,666.50			$12,666.50

*Assume that this item was consumed during the period of liquidation.

(Pp. 281–282); G. I, 63–64, 105–107; G. II, 70–72; E., 476–490.

SOLUTIONS TO EXERCISES

CHAPTER XIV

COST ACCOUNTS

Group One

1. *What is the purpose of Cost Accounts?*

1. The purpose of Cost Accounts is to ascertain either the total cost of production, or better, the *unit* cost of production. Modern business competition makes it imperative that the manufacturer and trader know exactly what it costs to produce an article; hence, it is necessary that records be kept from which may be ascertained definitely and positively the costs required.

(Pp. 291, 304); N., 19–23; H., 293–294; C. C., 1–4; B. M., Jan. 1903, 86–91.

2. *Distinguish between* post mortem *and contemporaneous Cost Accounts. (Prof. John R. Wildman, C. P. A., New York University School of Commerce, Accounts and Finance, calls the first Accounting Cost System, and the other Factory Cost System.)*

2. By *post mortem* Cost Accounts are meant accounts drawn off at the end of a year, or sometimes at the end of a half year, by means of which the cost of units or of total output is ascertained. Contemporaneous Cost Accounts make possible the ascertaining of these facts at much shorter intervals; usually weekly or monthly. In order to secure the information resulting from *post mortem* accounts, it is only necessary that the usual double entry books with proper

classifications be kept. For contemporaneous Cost Accounts a system supplementary to the usual double entry one is requisite, *viz.*, records to show materials consumed for various jobs; payroll allocation so as to apportion direct labor to the various jobs and activities; methods of distributing the factory burden or overhead according to various schemes, some of which have been outlined in Elements of Accounting, pages 315-317; and finally, a system of controlling accounts in the general Ledger. To sum up, therefore, the difference between the *post mortem* and contemporaneous systems is to be found in the fact that the former is more liable to error and is a grosser determination; whereas the latter is a more refined process and gives results in time to prevent serious losses (the stopping of leaks).

(P. 304.)

3. *How is the amount of direct wages ascertained?*

3. There are various means in use for the purpose of making possible determination of how much wages have been paid on account of each separate job. Essentially, each system contains these elements: the keeping of daily time, by timekeepers; the charging of each day's time to the job benefited; the aggregating of time of all laborers employed on the same job; the proof of the summary by comparing the total amount charged to each separate job with the total payroll for the period under review.

(P. 313); G. F., 21–23; A., 64–65; J., Vol. 18, 38–46.

4. *Describe the Stores Record. What are its functions?*

4. The Stores Record is usually a specially ruled ledger card, so arranged as to show the receipt of goods in the store room, disbursements of the same goods from the store room and the balance which should be on hand. The foregoing description gives the essentials of the stores record which is

illustrated by the form shown on page 309 of Elements of Accounting. Besides serving as a control of the goods on hand, it may also serve the following useful purposes:

(*a*) Value of goods purchased as well as physical quantities received; (*b*) value of goods disposed as well as physical quantities distributed; (*c*) balance on hand, not only in terms of physical units, but also in terms of value, and hence a perpetual inventory; (*d*) it is also useful as a constant reminder to the stores-keeper not to allow his stock on hand to run below a certain amount and never to order more than a certain amount.

(Pp. 308–309); N., 307–310; H., 310–311.

5. *Show how the Materials Purchased Account and the Manufacturing Account of the General Ledger are controlling accounts of the Cost Ledger.*

5. The Materials Purchased Account or the Merchandise Purchased Account is the controlling account for the first or "Materials Consumed" column of the Cost Sheet. The control is effected in the following way: the Purchases Account is debited for net purchases, usually once a month from the Purchase Book. Requisitions on the Storekeeper are entered in the Materials Record book kept for that purpose. The total of all goods requisitioned during the month may be found by totaling the requisitions issued and honored during the month, which, incidentally, must correspond to the total of all the charges for materials consumed against the individual job numbers as shown on the Materials Record. Once a month the total of the materials consumed by each job, as shown on this Materials Record, is posted to the first column on the Cost Sheet for the particular job for which the goods were ordered. Also, once a month the following Journal entry is made and posted:

Manufacturing Account	**$———**	
To Materials Purchased		**$———**

(Goods in Process Account is frequently debited instead of Manufacturing Account.) This debit to Goods in Process or to Manufacturing Account corresponds to the total of the monthly entries on all the Cost Sheets in the Materials Consumed column, and hence, the control is manifest.

Once a month the analysis of the Payroll Book is completed, and the direct wages chargeable against the separate jobs are entered to their respective cost sheets into the second or Wages Paid column. At the same time the following Journal entry is made and posted:

Manufacturing Account	$———	
To Wages		$———

(The charge might have been made, as before, to Goods in Process Account; the credit would be made to the account which was charged originally, such as Direct Wages Account, Labor Account, Factory Labor Account, etc.)

Once a month all the other factory expenses, including the unapportioned balance in the Wages or Labor Account, is distributed on the basis of materials consumed, or direct wages paid, or on prime costs. The amounts chargeable to each one of the jobs are then entered on their respective Cost Sheets in the third or Factory Overhead column. At the same time, that is, once a month, the following Journal entry is made:

Manufacturing Account	$———	
To Wages		$———
Factory Salary		———
Factory Supplies		———
Fuel		———
Oil		———
Etc., etc.		———

(The credits are for the purpose of removing from the various accounts to which the separate items or Factory Burden or Factory Overhead have been charged originally, such a portion as has actually been consumed or used up during the current month. The balances in each one of these Overhead

Accounts should then represent the unconsumed portion or Inventory. At this time the Manufacturing Account will be charged with three items: The first two, Materials Consumed and Direct Labor, will constitute Prime Cost, while the third item will be the other factory expenses, the three together constituting the total cost of manufacturing all goods during the entire month. Now, this Manufacturing Account which appears in the General Ledger [or Goods In Process Account after it has been transferred to the Manufacturing Account by an appropriate Journal entry] is the controlling account for the corresponding month of all the Cost Sheets in the Cost Ledger. This is so because the sum of the three columns for each month on any one Cost Sheet will constitute the total cost of manufacturing during that month for the job in question. The sum of the corresponding items on all of the Cost Sheets will, of course, constitute the total cost of manufacturing for all of the jobs during any given month, so that the control by means of the Manufacturing Account in the General Ledger must be clear.)

6. *What is Manufacturing Overhead? How is it apportioned?*

6. Manufacturing Overhead, or Factory Overhead, or Factory Burden, or Burden, or On Cost, is the term applied to that part of the Manufacturing Cost of production which is not Prime Cost. It therefore constitutes all items of expenditure or cost involved in the factory production other than materials consumed, freight inward and direct labor costs. Or, more positively, it consists of indirect factory labor, superintendence, fuel and oil consumed, factory supplies, depreciation of machinery and tools, factory taxes (water rates), heat and light, etc. Inasmuch as most concerns find it impracticable to ascertain positively the overhead charges for each job, the apportionment is usually left for the end of the period, that is, for the end of the week or for the end

of the month. The question then arises how much of the Factory Overhead should be borne by each one of the jobs. There is no unanimity of opinion as to the best means of apportioning this Overhead; and all familiar with this subject recognize the topic to be the most uncertain and unsatisfactory in the entire subject of Cost Accounting. But the Overhead must be apportioned, and we have already suggested three methods, viz.: on the basis of Direct Wages, or on the basis of Materials Consumed, or on the basis of Prime Cost. Advanced books on the subject discuss other methods, and to such advanced works the reader must be referred.

(Pp. 295, 314–317); N., 25–26, 54–69; H., 295–306.

Group Two

1. *The following problem is based on a recent examination question set by the New York C. P. A. examination board: The output of the Pennsylvania Coal Co. for 1911 was 100,000 tons, and the Trial Balance at the end of the year was:*

Trial Balance

Plant and Machinery	$50,000.00	Capital Stock	$80,000.00
Construction	10,000.00	Sales	158,500.00
Notes and Accounts Receivable	38,000.00	Notes and Accounts Payable	18,000.00
Cash	15,000.00		
Mine Supplies	6,000.00		
Inventory Coal, 1/1/1911 *	12,000.00		
Wages	60,000.00		
Salaries (office)	13,000.00		
Accident Insurance	5,000.00		
Water Taxes	1,000.00		
Office Expenses	11,000.00		
Freight Outward	10,000.00		
Stable Expense (mine)	7,500.00		
General Expenses	18,000.00		
	$256,500.00		$256,500.00

* Last year's mining cost was 80¢ per ton.

The inventory of coal on hand ready for shipment was $16,500.00.

Write off 10% depreciation from Plant and Machinery Account.

(*a*) *Prepare a Profit and Loss and Income Statement showing the unit cost and percentage figures you deem desirable.*

(*b*) *Also prepare a Balance Sheet.*

1 (*a*)

Profit and Loss and Income Statement of the Pennsylvania Coal Company

FOR THE YEAR ENDED DECEMBER 31, 1911

					Per Cent	Cost Statistics	
Net Sales, 95,474 tons @ $1.66			$158,500	00	100.0	1	66
Cost of Mining:							
Wages	$60,000.00						
Mine Supplies	6,000.00						
Accident Insurance	5,000.00						
Water Taxes	1,000.00						
Stable Expense	7,500.00						
Depreciation	5,000.00						
Cost of mining 100,000 tons		$84,500.00					
Add inventory Jan. 1, 1911: 15,000 tons @ 80c		12,000.00					
		$96,500.00					
Deduct inventory Dec. 31, 1911: 19,526 + tons @ 84½c		16,500.00					
MINING COST OF 95,474 TONS			80,000	00	50.4		83
Gross Profit on Mining			78,500	00			
Cost of Selling and Administration:							
Salaries	$13,000.00						
Office Expenses	11,000.00						
Freight Outward	10,000.00						
General Expenses	18,000.00						
Selling and Administration Cost			52,000	00	32.8		54
NET PROFIT			26,500	00	16.7		28

(b)

Balance Sheet of the Pennsylvania Coal Company

AS OF DECEMBER 31, 1911

ASSETS		LIABILITIES AND CAPITAL	
Cash	$15,000.00	Notes and Accounts Payable	$18,000.00
Notes and Accounts Receivable	38,000.00	Capital Stock	80,000.00
Inventory	16,500.00	Surplus	26,500.00
Plant and Machinery	45,000.00		
Construction	10,000.00		
	$124,500.00		$124,500.00

(Pp. 297–301); G. I, 97–104; G. II, 96–98, 132–134, 150–153.

2. *Fill in the cost sheet shown on page 312,* choosing your own figures, and prepare a chart showing the changes in the unit cost of production for the twelve months of the year.*

2. No solution is offered. It is suggested, however, that figures chosen should be such as to result in probable unit costs. Violent and extreme fluctuations do not usually occur in actual practice.

3. *Using Exercise 2 of Group Two, page 82, prepare a Profit and Loss and Income Statement similar to any one of those presented in Chapter XIII.* Assume that the Kent Manufacturing Company manufactures a patented fountain pen which it sells at the uniform wholesale price of $1.00 each. The sales for the year amounted to 57,770 pens, and there were manufactured during the year 60,000 pens.*

* Reference to Elements of Accounting.

3. Profit and Loss and Income Statement of the Kent Manufacturing Company

FOR THE PERIOD ENDED DECEMBER 31, 1913

					Per Cent	Cost Statistics
Sales, 57,770 pens @ $1.00		$57,770.00				
Less Returned Sales, 1,200 pens @ $1.00	$1,200.00					
Discount on Sales	310.00	1,510.00				
NET SALES, 56,570 pens			56,260	00	100.0	99
Deduct Cost of Manufacturing:						
Prime Cost:						
Raw Materials (1/1/13)		$3,000.00				
Purchases		20,000.00				
Wages (including accrued $120.00)		8,320.00				
		$31,320.00				
Less Returned Purchases	$1,000.00					
Inventory Raw Materials (12/31/13)	3,600.00					
Inventory Goods in Process (12/31/13)	4,500.00	9,100.00				
PRIME COST of 60,000 pens		$22,220.00				37
Factory Overhead:						
Fuel	$2,200.00					
Factory Salary	3,200.00					
Depreciation on Plant and Mach.	1,000.00					
Depreciation on Tools	200.00					
Factory Insurance	70.00					
Factory Expense	1,300.00					
FACTORY OVERHEAD of 60,000 pens		7,970.00				13⅓
COST TO MANUFACTURE 60,000 pens		$30,190.00				50⅓
Add Inventory of pens on hand, 1/1/13: 8,097 @ $.49		4,000.00				
Less Inventory of pens on hand, 12/31/13: 11,527 @ $.50⅓		5,800.00				
MANUFACTURING COST of 56,570 pens sold			28,390	00	50.4	50
GROSS PROFIT ON SALES			27,870	00		
Deduct Selling and Administration Expenses:						
Freight Outward		$1,100.00				
Selling Expenses		7,300.00				
Commission		1,800.00				
Office Expense		2,150.00				
Office Salary		4,000.00				
COST OF SELLING AND ADMINISTRATION			16,350	00	29.0	29
GROSS BUSINESS PROFIT			11,520	00		
Other Deductions:						
Discount on Notes		$165.00				
Interest on Loans		300.00				
Bad Debts		470.00				
		$935.00				
Less Discount on Purchases		175.00				
TOTAL OTHER DEDUCTIONS			760	00	1.3	01
NET INCOME			10,760	00	19.1	19

SOLUTIONS TO EXERCISES

CHAPTER XV

AUDITING

Group One

1. *State the object to be attained by an audit.*

1. The object of any audit depends upon the purpose for which the auditor was engaged. The object of a general audit is to discover fraud or errors. In actual practice the scope of an audit is considerably broader than here indicated.

(Pp. 322–323); M., 8–11, 17–18; C., 281–283; G. II, 219.

2. *Why is an independent audit by a professional accountant desirable?*

2. There are three principal reasons why an independent audit should be favored. The point of view and experience of the professional auditor frequently results in suggestions for improvement which are worth considerably more than the cost of the services rendered. Where fraud is suspected, or where errors exist, none other than an independent professional auditor can be relied upon for the services required. For banks and for credit agencies the reports of independent professional auditors are practically mandatory.

M., 34–38; J., Vol. 10, 95–100.

3. *How can fraud in payment of wages be prevented?*

3. As in all other cases where fraud may occur, eternal vigilance is essential. One successful method of preventing fraud in connection with the payment of wages is to pursue the following plan:

(*a*) The timekeeping and the calculating of the amount of wages should be performed by different employees.

(*b*) Neither the person who acts as timekeeper nor the person who calculates the amount of wages should distribute payroll envelopes.

(*c*) The clerks who perform the various duties in connection with the payroll calculation and distribution should occasionally be shifted about without notice.

(*d*) Employees, before receiving their payroll envelopes, should be asked how much money they expect in order to check up the amount in the payroll envelopes.

(*e*) Whatever routine is adopted it should be changed occasionally, and without previous notice, so as to avoid falling into a rut. Such changes are most likely to reveal any evil practices.

(P. 342); M., 288–290

4. *Describe, in detail, how to audit the Cash Book.*

4. The following procedure will suffice for elementary purposes:

(*a*) The columns on both sides of the Cash Book should be added, particular attention being given to the transfer of totals and balances from page to page.

(*b*) The receipts entered in the Cash Book should be carefully checked with whatever evidences are available as vouchers. Such evidence may consist of carbon copies of receipts, letters of acknowledgment, and entries upon the credit side of customers' accounts in the Sales Ledger. The cash remittances of customers should be carefully checked from the Sales Ledger back to the Cash Book.

(*c*) The receipts should also be carefully checked with the daily bank deposit. Any tendency to hold back deposits, which such checking may reveal, should be carefully investigated.

(*d*) The discounts, which appear in the Discount on Sales column, should be tested. It should be observed that if the cashier were to increase the book entry for the discount he would be able to retain the excess discount added.

(*e*) The disbursement side of the Cash Book should be carefully compared with the canceled bank vouchers, check book stubs, and any other vouchers.

(*f*) The Creditors' Ledger, debit side, should be checked back to the payment side of the Cash Book.

(*g*) Decreasing the book entry for the amount of actual discount taken would enable the cashier to retain the difference. Accordingly, the Discount on Purchases column should be tested.

(*h*) Finally, the cash balance should be reconciled with the bank balance.

(Pp. 324–326, 338–340); M., 252–255; R., 36–41; D. A., 17–25.

5. *What is a Working Sheet? How is it employed?*

5. A Working Sheet is one of the auditor's most useful tools. It is essentially a journal sheet containing extra money columns. It is employed by the auditor to copy balances, to make rough notes of adjustments necessitated by discovery of errors or the existence of inventories, etc. It also contains any memoranda which will serve to remind him of matters which should be investigated, and of items to be included in the final report. Additional columns on the Working Sheet are employed for the purpose of making a preliminary draft from which to prepare the Balance Sheet and Income Statement.

(Pp. 328–331, 342–343, 346–347); M., 73–77.

6. *Can the auditor tell whether the inventory submitted to him is correct or not? How?*

6. The auditor can usually test the correctness of the merchandise inventory submitted to him. By ascertaining the percentage of profit on sales or on Turnover, he can frequently establish the approximate amount of the inventory. He can also ascertain whether the unit prices shown upon the inventory sheets are reasonable in terms of cost or market price. Except in rare cases he is not in the position to certify to the physical existence of the goods listed in the inventory. He should make sure, however, that goods held on consignment, unmarketable goods and goods which have as yet not been credited to accounts in the Purchase Ledger, are not included in the inventory.

(Pp. 326–327); M., 107–113; G. I, 204; G. II, 228; J., Vol. 12, 352–356.

7. *Mention some of the services the auditor may render the business community.*

7. In actual practice the auditor installs systems of accounts and reviews the work of the bookkeeper. He makes suggestions for decreasing cost, and in this way benefits the entire community by making possible a lower price. His activities tend to eliminate waste and extravagance in municipal, state and national governments, and in public and in quasi-public corporations. Because of his experience and point of view, he is frequently consulted by business men in relation to financial disputes, questions of business policy, etc., etc. He also prepares statements for trustees and executors, and tax statements for corporations and individuals.

See references for Exercise 1, above.

8. *What is the difference between a special examination and a complete audit?*

8. The complete audit comprises the examination of all vouchers, books and records, for the purpose of detecting errors and fraud. and leading up to the preparation of the Balance

Sheet, Income Statement, and, sometimes, the offering of suggestions for improvement in office routine, etc. The special examination is for the purpose of ascertaining some definite point, and is consequently limited by the particular purpose for which the examination is conducted. Though the examination is as thorough *per se* as the complete audit, it differs from the latter in that its scope is much narrower.

M., 502–503; G. I, 207; G. II, 227.

9. *Mention the preliminary steps necessary to organize the accounting system of a manufacturer of hats.*

9. For the present purpose the following outline is sufficient:

(*a*) The probable activities of the concern should be carefully surveyed, for the purpose of ascertaining what transactions will occur.

(*b*) A sort of quantitative analysis should then be made so as to ascertain the relative importance of the various kinds of transactions in order to provide labor-saving devices for the more frequently occurring transactions.

(*c*) Before ordering books and forms it is well to record upon rough drafts the anticipated transactions, or those which have actually occurred, in order to test the value of the proposed system.

(*d*) Detailed instruction should be left with the office staff so as to avoid misunderstanding and error.

(*e*) Arrangements should be made for supervision during the early stages, so as to eliminate weak points as soon as developed, and in order to make sure that the instructions left are properly observed.

(Pp. 351–353); K., 1–6; M., 308–316, 525–527: D., 11–12; D. A., 65–74; S. O., 100–109; W.. 21–29; J., Vol. 5, 41–43.

Group Two

1. *Prepare the exhibits and the schedules omitted in Chapter XV, Elements of Accounting, page 350.*

1. Answer unnecessary.

2. *As the auditor for the National Burglary Protective Association, report on the claim of a member for loss by theft of $8,000.00 worth of furs. You derive the following information from his books:*

(a)	*Average profit on first cost during past three years, 25%.*	
(b)	*Inventory at beginning of year,*	*$18,500.00*
(c)	*Purchases during period*	*64,000.00*
(d)	*Sales during period*	*79,800.00*
(e)	*Present inventory*	*18,000.00*

2.

Original Inventory		$18,500.00
Purchases during period		64,000.00
		$82,500.00
Less:		
Present Inventory	$18,000.00	
Cost of Sales ($79,800 divided by 125%)	63,840.00	81,840.00
MAXIMUM LOSS		$660.00

I would report that according to the data submitted to me, the maximum loss, as per the foregoing exhibit, was $660.00. This loss might be decreased by further investigation, but enough has been disclosed to warrant the statement that the claim of loss has been grossly exaggerated.

(P. 327); G. II, 228.

3. *Prepare, from your own figures, a schedule of accounts receivable, dividing balances into those due within 30, 60, 90, and more days, respectively. Remember that some accounts may contain items falling into more than one class.*

3.

B. & D.

EXHIBIT A—SCHEDULE ONE

Accounts Receivable

L.F.	Customer	Balance		Current		30–60		60–90		Over 90 days	
1	Smith & Co.	375	50	375	50						
9	H. M. Rollins	1,200	00	710	00	490	00				
12	N. Y. Trading Co.	1,384	50	265	00	500	00	619	50		
18	National Dress Co.	984	68							984	68
27	E. M. Price	573	00	573	00						
58	Lange & Lange	1,898	00	1,898	00						
59	Simpson & Co.	659	32			659	32				
62	Brown Bros.	962	00	262	00	700	00				
63	Stern & Lyons	790	00					400	00	390	00
64	Kahn, Lee & Co.	380	00	380	00						
		9207	00	4,463	50	2,349	32	1,019	50	1,374	68

M., 94–96.

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